

EIGHTEENTH CONGRESS OF THE)
REPUBLIC OF THE PHILIPPINES)
First Regular Session)



Senate
Office of the Secretary

19 SEP 16 P1:36

SENATE

S. No. 1050

RECEIVED BY:

Introduced by Senator Ralph G. Recto

AN ACT
EXEMPTING DIVIDENDS FROM INCOME TAX AND ABOLISHING THE
IMPROPERLY ACCUMULATED EARNINGS TAX, AMENDING FOR THIS
PURPOSE SECTIONS 24(B), 25(A), 32(B) AND 57(A), AND REPEALING
SECTION 29 OF THE NATIONAL INTERNAL REVENUE CODE OF 1997, AS
AMENDED

EXPLANATORY NOTE

This proposed measure seeks to exempt dividends from income tax and abolish the improperly accumulated earnings tax.

The tax on dividends has been previously abolished in a gradual manner through Executive Order (EO) No. 37 which took effect on August 1, 1986 and provides that dividends received from a domestic corporation and the share of an individual partner from a partnership shall be subject to tax at the rate of 15% effective in 1986; 10% effective January 1, 1987; 5% effective January 1, 1988; and 0% effective January 1, 1989. However, the National Internal Revenue Code (NIRC) of 1997 reintroduced the tax on dividends in our jurisdiction and imposed a final tax of 6% beginning January 1, 1998; 8% beginning January 1, 1999; and 10% beginning January 1, 2000.

The concept of improperly accumulated earnings tax (IAET) has been in our income tax system since the NIRC of 1939. However, it was abolished in 1986 through EO 37, but was later on reintroduced in the NIRC of 1997. The 10% IAET is

imposed on the improperly accumulated taxable income of every corporation formed or availed for the purpose of avoiding the income tax with respect to its shareholders or the shareholders of any other corporation.

The tax on improper accumulation of surplus is essentially a penalty tax designed to compel corporations to distribute earnings so that the said earnings by shareholders could, in turn, be taxed.¹

Under the Revised Corporation Code, a duly organized corporation is clothed with a personality separate and distinct from the persons composing it. This separate and distinct personality of corporations justifies their being subject to taxation in many jurisdictions. For this reason, the earnings of a corporation may be subjected to different kinds of taxes.

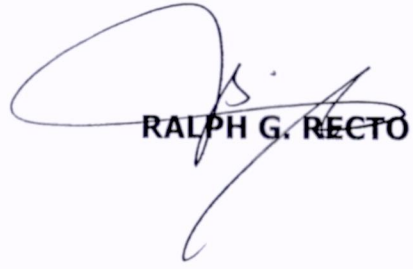
In our jurisdiction, the revenues generated by every corporation may be subjected to either the value-added tax (VAT) or percentage tax and the same revenue is also subject to local business tax. The taxable net income of a corporation is subject to corporate income tax and the same net income once declared and distributed as dividends, the recipient shareholders also pay a final tax.

The imposition of tax on dividends disincentivizes businessmen and investors to further expand their businesses through the establishment of a corporation. Taxing twice the same income stream of a corporation would constitute inequitable distribution of tax burden.

Hence, exempting dividends from income tax is only fair, just and reasonable to minimize the inequity in tax burden sharing between and among all subjects of taxation. This is in line with the constitutional mandate that the rule of taxation shall be uniform and equitable. Likewise, abolishing IAET is only proper for it serves no purpose at all if dividends are no longer subject to income tax.

¹ Cyanamid Philippines, Inc. vs. The Court of Appeals, G.R. No. 108067, January 20, 2000

In view of the foregoing, the approval of this bill is earnestly sought.



RALPH G. RECTO

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SECTION 29 OF THE NATIONAL INTERNAL REVENUE CODE OF 1997, AS
AMENDED

Be it enacted by the Senate and House of Representatives of the Philippines in Congress assembled:

1 Section 1. Section 24(B) of the National Internal Revenue Code of 1997, as
2 amended, is hereby further amended to read as follows:

3 "SEC. 24. *Income Tax Rates.* –

4 "(A) xxx

5 "xxx

6 "(B) *Rate of Tax on Certain Passive Income:* –

7 "(1) xxx

8 "~~[(2) *Cash and/or Property Dividends.*—A final tax at the rate of ten~~
9 ~~percent (10%) shall be imposed upon the cash and/or property dividends~~
10 ~~actually or constructively received by an individual from a domestic~~
11 ~~corporation or from a joint stock company, insurance or mutual fund~~
12 ~~companies and regional operating headquarters of multinational companies,~~
13 ~~or on the share of an individual in the distributable net income after tax of a~~
14 ~~partnership (except a general professional partnership) of which he is a~~
15 ~~partner, or on the share of an individual in the net income after tax of an~~

1 association, a joint account, or a joint venture or consortium taxable as a
2 corporation of which he is a member or co-venturer.]

3 "xxx"

4 Sec. 2. Section 25(A) of the National Internal Revenue Code of 1997, as
5 amended, is hereby further amended to read as follows:

6 "SEC. 25. *Tax on Nonresident Alien Individual.* –

7 "(A) *Nonresident Alien Engaged in Trade or Business Within the*
8 *Philippines.* –

9 "(1) xxx

10 "(2) [~~Cash and/or Property Dividends from a Domestic Corporation or~~
11 ~~Joint Stock Company, or Insurance or Mutual Fund Company or Regional~~
12 ~~Operating Headquarter of Multinational Company, or Share in the~~
13 ~~Distributable Net Income of a Partnership (Except a General Professional~~
14 ~~Partnership), Joint Account, Joint Venture Taxable as a Corporation or~~
15 ~~Association;]~~ *Interests, Royalties, Prizes, and Other Winnings.* – [Cash
16 and/or property dividends from a domestic corporation, or from a joint stock
17 company, or from an insurance or mutual fund company or from a regional
18 operating headquarter of multinational company, or the share of a
19 nonresident alien individual in the distributable net income after tax of a
20 partnership (except a general professional partnership) of which he is a
21 partner, or the share of a nonresident alien individual in the net income after
22 tax of an association, a joint account, or a joint venture taxable as a
23 corporation of which he is a member or a co-venturer; i] **I**nterests; royalties
24 (in any form); and prizes (except prizes amounting to Ten thousand pesos
25 (P10,000) or less which shall be subject to tax under Subsection (B)(1) of
26 Section 24) and other winnings (except Philippine Charity Sweepstakes and
27 Lotto winnings), shall be subject to an income tax of twenty percent (20%)
28 on the total amount thereof: *Provided, however,* That royalties on books as
29 well as other literary works, and royalties on musical compositions shall be
30 subject to a final tax of ten percent (10%) on the total amount thereof:
31 *Provided, further,* That cinematographic films and similar works shall be
32 subject to the tax provided under Section 28 of this Code: *Provided,*

1 *furthermore*, That interest income from long-term deposit or investment in
2 the form of savings, common or individual trust funds, deposit substitutes,
3 investment management accounts and other investments evidenced by
4 certificates in such form prescribed by the Bangko Sentral ng Pilipinas (BSP)
5 shall be exempt from the tax imposed under this Subsection: *Provided, finally*,
6 That should the holder of the certificate pre-terminate the deposit or
7 investment before the fifth (5th) year, a final tax shall be imposed on the
8 entire income and shall be deducted and withheld by the depository bank
9 from the proceeds of the long-term deposit or investment certificate based on
10 the remaining maturity thereof:

11 Four (4) years to less than five (5) years - 5%;

12 Three (3) years to less than four (4) years - 12%; and

13 Less than three (3) years - 20%.

14 "(3) xxx

15 "xxx"

16 Sec. 3. Section 29 of the National Internal Revenue Code of 1997, as
17 amended, is hereby repealed and the succeeding sections are hereby renumbered
18 accordingly.

19 Sec. 4. Section 32(B) of the National Internal Revenue Code of 1997, as
20 amended, is hereby further amended to read as follows:

21 "SEC. 32. *Gross Income.* –

22 "(A) xxx

23 "xxx

24 "(B) *Exclusions from Gross Income.* – The following items shall not be
25 included in gross income and shall be exempt from taxation under this Title:

26 "(1) xxx

27 "xxx

28 "(7) *Miscellaneous Items.* –

29 "(a) xxx

30 "(h) xxx

31 "(I) ***DIVIDENDS.*** – **CASH AND/OR PROPERTY DIVIDENDS**
32 **ACTUALLY OR CONSTRUCTIVELY RECEIVED BY AN INDIVIDUAL**

1 (EXCEPT A NONRESIDENT ALIEN INDIVIDUAL NOT ENGAGED IN
2 TRADE OR BUSINESS WITHIN THE PHILIPPINES) AND A
3 CORPORATION (EXCEPT A NONRESIDENT FOREIGN CORPORATION)
4 FROM ANOTHER CORPORATION, OR FROM A JOINT STOCK
5 COMPANY, OR FROM AN INSURANCE OR MUTUAL FUND COMPANY
6 OR FROM A REGIONAL OPERATING HEADQUARTERS OF A
7 MULTINATIONAL COMPANY, OR THE SHARE OF AN INDIVIDUAL IN
8 THE DISTRIBUTABLE NET INCOME AFTER TAX OF A PARTNERSHIP
9 (EXCEPT A GENERAL PROFESSIONAL PARTNERSHIP) OF WHICH HE
10 IS A PARTNER, OR THE SHARE OF AN INDIVIDUAL IN THE NET
11 INCOME AFTER TAX OF AN ASSOCIATION, A JOINT ACCOUNT, OR A
12 JOINT VENTURE TAXABLE AS A CORPORATION OF WHICH HE IS A
13 MEMBER OR A CO-VENTURER.”

14 Sec. 5. Section 57(A) of the National Internal Revenue Code of 1997, as
15 amended, is hereby further amended to read as follows:

16 “SEC. 57. *Withholding of Tax at Source.* –

17 “(A) *Withholding of Final Tax on Certain Incomes.* – Subject to rules
18 and regulations the Secretary of Finance may promulgate, upon the
19 recommendation of the Commissioner, requiring the filing of income tax
20 return by certain income payees, the tax imposed or prescribed by Sections
21 24(B)(1), [~~24(B)(2);~~] 24(C), 24(D)(1); [~~25(A)(2);~~] 25(A)(3), 25(B), 25(C),
22 25(D), 25(E); 27(D)(1), 27(D)(2), 27(D)(3), 27(D)(5); 28 (A)(4), 28(A)(5),
23 28(A)(7)(a), 28(A)(7)(b), 28(A)(7)(c), 28(B)(1), 28(B)(2), 28(B)(3), 28(B)(4),
24 28(B)(5)(a), 28(B)(5)(b), 28(B)(5)(c); 33; and 282 of this Code on specified
25 items of income shall be withheld by payor-corporation and/or person and
26 paid in the same manner and subject to the same conditions as provided in
27 Section 58 of this Code.

28 “xxx”

29 Sec. 6. *Implementing Rules and Regulations (IRR).* – Within thirty (30) days
30 from the effectivity of this Act, the Secretary of Finance, upon the recommendation
31 of the Commissioner of Internal Revenue, shall promulgate the necessary rules and
32 regulations for its effective implementation.

1 Sec. 7. *Separability Clause.* – If any provision or part hereof is declared
2 unconstitutional, the remainder of this Act or any provision not affected shall remain
3 in full force and effect.

4 Sec. 8. *Repealing Clause.* – All laws, acts, decrees, executive orders,
5 issuances, and rules and regulations or parts thereof which are contrary to and
6 inconsistent with this Act are hereby repealed, amended or modified accordingly.

7 Sec. 9. *Effectivity.* – This Act shall take effect fifteen (15) days after its
8 complete publication in the *Official Gazette* or in at least two (2) newspapers of
9 general circulation.

 Approved,