

TAXATION ON INVESTMENTS IN PHILIPPINES MARKET

Prepared by: Pintu Roy

Reviewed by: Vishal Chhablani

Document Version: 1.0



Table of Content

1. Executive Summary.....	2
2. Taxation in Philippines Market - Overview	3
Taxes Applicable 1.....	5
Taxes Applicable 2.....	6
3. Taxation Matrix	7
3.1 Taxable Securities.....	7
3.2 Tax Paid Securities.....	7
3.3 Tax Free Securities	7
4. Tax Exemption on Long Term Investments	9
5. Test Cases and Accounting.....	10
6. References.....	11
Calculation of WHT	12
Fixed Deposit.....	13
Special Deposit Account.....	14
7. Version History.....	15



1. Executive Summary

Taxation is a way of raising income in order to defray the necessary expenses of the government. It is the inherent power of the state to demand contribution to finance all the government expenses.

A tax is a financial charge imposed upon a taxpayer by a state or the functional equivalent of a state such that failure to pay, or evasion of or resistance to collection, is punishable by law.

In Philippines, all types of taxes are controlled by and paid to the Bureau of Internal Revenue (BIR).

A different type of Tax on investments is applicable in Philippines market which is not seen in most other countries. It is known as Withholding Tax (WHT). WHT is a tax levied on income (interest and dividends) from securities, and paid directly to the BIR. So the issuer deducts the WHT first before paying the interest to the investor.

The financial instruments are classified into following 3 categories:-

- Tax Paid - Investor will pay the tax upfront while doing transaction
- Taxable - Investor will pay the tax later on a future date
- Tax Free - No tax is paid by the investor

iDeal Funds and iDeal Wealth have the provision to calculate WHT on investments. These products can be offered as solutions for any requirement regarding WHT.

The method for calculating WHT is different for various types of asset classes. Test Cases with illustration of steps on how to calculate WHT have been provided in this document for Coupon bearing securities, discounted securities, Fixed Deposit, Special Deposit Account and Equity. Also the accounting entries at deal level have been shown for both Tax Paid and Tax Free securities.

2. Taxation in Philippines Market - Overview

- The Bureau of Internal Revenue (Filipino: Kawanihan ng Rentas Internas, or BIR) is an attached agency of Department of Finance. BIR collects all the taxes on behalf of the Philippines government. Kim Henares is the current Commissioner of BIR.
- There are many different kinds of taxes on Investments in the Philippines market. They are detailed as below:
- Documentary Stamp Tax (DST) – is a tax on documents, instruments, loan agreements and papers evidencing the acceptance, assignment, sale or transfer of an obligation, rights, or property incident thereto. Examples of documentary stamp tax are those that are charged on bank promissory notes, deed of sale, and deed of assignment on transfer of shares of corporate stock ownership.
- Value Added Tax (VAT) – is a business tax imposed and collected from the seller in the course of trade on every sale of security. It is an indirect tax, thus, it can be passed on to the buyer, causing this to increase the prices of securities bought and paid by buyers. VAT returns are usually filed and paid monthly and quarterly.
- Withholding Tax (WHT) – is the tax applicable in Philippines market, also called a retention tax, and is a government requirement for the payer on an investment income to withhold or deduct tax from the payment, and pay that tax to the BIR. This ensures the taxes are paid first before the money can be spent for any other purpose.
- Expanded Withholding Tax (EWHT) – is a kind of withholding tax which is prescribed only for certain payers and is creditable against the income tax due of the payee for the taxable quarter year. Examples of the expanded withholding taxes are those that are withheld on rental income and professional income.
- Final Withholding Tax (FWHT) – is a kind of withholding tax which is prescribed only for certain payers and is not creditable against the income tax due of the payee for the taxable year. Income Tax withheld constitutes the full and final payment of the Income Tax due from the payee on the said income. An example of final withholding tax is the tax withheld by banks on the interest income earned on bank deposits.
- Withholding Tax on Government Money Payments – is the withholding tax withheld by government offices and instrumentalities, including government-owned or -controlled corporations and local

government units, before making any payments to private individuals, corporations, partnerships and/or associations.

- Sales Tax – is the tax applied only in case of Sale of securities.
- Tax on Dividend – 10% tax is applied on dividends if the receiver is an individual. In case of Corporate there is no tax on dividend.

Please refer the attached sheets 'Taxes Applicable 1' and 'Taxes Applicable 2' for the Tax details.



Taxes Applicable
1.xlsx



Taxes Applicable
2.xlsx



Taxes Applicable 1

	Doc. Stamp Tax (DST)	Withholding Tax	Expanded Withholding Tax	Value Added Tax	Sales Tax
Investor Servicing					
Subscriptions	No. of Shares Subscribed /200				
Redemption	None				
Commission given to Distributor			10%	12% input VAT (only for computation purposes)	
Investments					
Savings		PHP - 20% USD - 7.5%			
Time Deposits		PHP - 20% USD - 7.5%			
Time Deposits - Pretermination	(PHP Principal/200) X (Original Tenor/360)	PHP - 20% USD - 7.5%			
Borrowing	(U\$D Loan Principal x FX rate)/200) X (Original Tenor / 365) (Php Loan Principal/ P200) X (Original Tenor/ 365)	USD - 10% PHP - 20%			
Equities			10% of broker's commission	12% - VAT on Commission	0.5% only for Equity Sale
PHP Bonds		20%			
USD Bonds		7.5%			

Taxes Applicable 2

Currency	Asset Class	Event	WHT	EWHT	VAT	DST	Any Other Tax
PHP	Fixed Deposit	Interest Income	20%	NA	NA	NA	
USD	Fixed Deposit	Interest Income	7.50%	NA	NA	NA	
PHP	Fixed Deposit	Premature Withdrawal	20%	NA	NA	(Principal/200) * (Original Tenor/360)	
USD	Fixed Deposit	Premature Withdrawal	7.50%	NA	NA	NA	
PHP	Bonds	Interest Income	20%	NA	NA	NA	
USD	Bonds	Interest Income	7.50%	NA	NA	NA	
PHP	Borrowing	Interest Income	20.00 %	NA	NA	(PHP Loan Principal/P200) X (Original Tenor/365)	
USD	Borrowing	Interest Income	10.00 %	NA	NA	(USD Loan Principal x FX rate)/200) X (Original Tenor / 365)	
PHP	Equity	Purchase and Sale	NA	10% of Brokerage	12% on Brokerage	NA	Sales Tax - 0.5% of Book Value (Applicable only for Equity Sale Transaction)
PHP	NA	Management fee	NA	15%	NA	NA	NA
USD	NA	Management fee	NA	15%	NA	NA	NA
PHP	NA	Subscription	NA	NA	NA	No. of Shares Subscribed/200	NA
USD	NA	Subscription	NA	NA	NA	No. of Shares Subscribed/200	NA
PHP	NA	Distributor Commission	NA	10%	12% of Taxable Commission	NA	NA

3. Taxation Matrix

In Philippines, both the Client and the Security are classified as Taxable, Tax paid or Tax Free. They are described as below:-

3.1 Taxable Securities

In Taxable Securities, Issuer pays full interest amount to the client who holds the security on interest payment date. If the client is “Taxable” he will pay tax amount on interest earned to the government, whereas if the client is “Tax-exempted” need not pay any tax on income.

3.2 Tax Paid Securities

In Tax Paid Securities, Issuer pays interest net of tax amount to client irrespective of client is “Taxable” or “Tax-exempted”. Issuer also provides a reference no. to the client for tax paid to the government. If client is “Taxable” he needs to inform the government for tax paid by the issuer using reference no., whereas if client is “Tax-exempted” then using reference no. provided by issuer he can claim tax amount from the government.

3.3 Tax Free Securities

In Tax Free Securities, Issuer pays full interest amount to the client who holds the security on interest payment date irrespective of client’s tax status.

The Trust Business in Philippines takes into consideration two aspects while calculating the tax which are **Client Account Tax Status** and **Security Tax Status**. It has been explained through a Taxation Matrix which has 6 different scenarios.

Tax Matrix

Client Account Tax Status	Security Tax Status		
	Taxable	Tax paid	Tax exempt
Taxable	P	P	E
Tax exempt	E	P	E

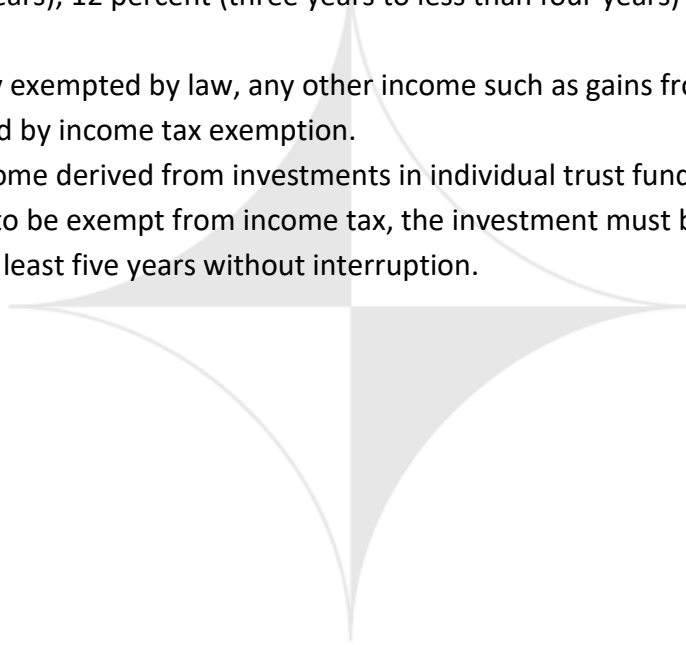
'T' - Taxable, 'P' - Tax Paid, 'E' - Tax Exempt

Exception Scenario






- **Gross receipt tax (GRT)** applicable only on SDA (Special Deposit Accounts) with effect from 1st august 2014 @ 5% is mandatory irrespective of any status in above Tax Matrix. For e.g. Tax Exempted SDA security will also have an impact of 5% GRT whereas for Taxable SDA security 5% GRT will be applied along with other taxes.
- Tax on Dividend of Preference Stock is calculated for every 90 days, irrespective of the purchase duration. In case the client has bought the security 45 days before the next Dividend date, tax that has to be paid will be for the entire duration i.e. 90 days.

4. Tax Exemption on Long Term Investments

- The Bureau of Internal Revenue reiterated that interest earnings from long-term deposits or investments are exempted from income tax as long as these have a maturity period of not less than five years.
- The deposits or investments covered by this rule are time deposits or investments in the form of savings, common or individual trust funds, deposit substitutes and investment management accounts.
- The income tax exemption can only be enjoyed by depositors that are individual citizens or aliens engaged in trade or business in the Philippines.
- The long-term deposits or investments must be issued by banks only and not by other entities or individuals. These must also be issued by banks in denominations of PHP 10,000.
- Moreover, these deposits should not be terminated before end of the fifth year otherwise they shall be subjected to the graduated withholding tax rates based on the age of the deposit – five percent (four years to less than five years), 12 percent (three years to less than four years) and 20 percent (less than three years).
- Except those specifically exempted by law, any other income such as gains from trading, foreign exchange gain shall not be covered by income tax exemption.
- In order for interest income derived from investments in individual trust funds or investment management accounts to be exempt from income tax, the investment must be managed by the bank for the named individual at least five years without interruption.



5. Test Cases and Accounting

<p>1) Coupon bearing security (Tax Paid, Taxable and Tax Exempt):</p> <p>a) Test case shows the WHT calculation on Corporate Bond.</p> <p>b) Accounting Entries</p>	 <p>WHT Corporate Bond.xlsx</p>
<p>2) Discounted instrument (Tax Paid, Taxable and Tax Exempt):</p> <p>a) Test case shows the WHT calculation on Treasury Bills.</p> <p>b) Tax is been deducted on upfront basis for Tax Paid T-Bills.</p>	 <p>WHT Tbills.xlsx</p>
<p>3) Fixed Deposit:</p> <p>a) Test case shows the WHT calculation on Fixed Deposit.</p> <p>b) Tax deduction on Fixed/Term Deposit is calculated upfront.</p>	 <p>WHT FD.xls</p>
<p>4) Special Deposit Account (SDA):</p> <p>a) Test case shows the WHT calculation on SDA.</p> <p>b) Tax on SDA is calculated on upfront basis.</p>	 <p>WHT SDA.xls</p>
<p>5) Equity</p> <p>a) Test case shows the WHT calculation on Equity securities.</p> <p>b) In Equity dividend the WHT is 10% for individuals and for corporate it is exempted.</p>	 <p>WHT Equity.xls</p>

6. References

- 1) www.philstar.com
- 2) www.imf.org
- 3) www.bir.gov.ph
- 4) www.wikipedia.org
- 5) www.investopedia.com



Calculation of WHT

Sr. No.	Steps to calculate the WHT	Tax Paid Security	Taxable/Tax Free Security	Remarks
1	Deduct the WHT from the Gross Coupon Rate of the security to find its Net Coupon Rate	<u>Net Coupon</u>	<u>Net Coupon</u>	Net Coupon Rate for Taxable/Tax Free Security will be same as its Gross Coupon Rate.
2	Calculate the Gross Yield from Gross Coupon Rate	<u>Gross Yield</u>	<u>Gross Yield</u>	
	Calculate the Net Yield from Net Coupon Rate	<u>Net Yield</u>	<u>Net Yield</u>	Net Yield will be equal to Gross Yield for Taxable/Tax Free Security.
3	Calculate the Gross Price from Gross Yield	<u>Gross Price</u>	<u>Gross Price</u>	
4	Calculate the Net Price from Net Yield.	<u>Net Price</u>	<u>Net Price</u>	Inverse Relation between yield and price may not hold true because of the change in cash flows due to change in coupon rate.
5	Find the accrued interest, if any, and calculate the Net Interest	<u>Net Interest</u>	<u>Net Interest</u>	
6	Calculate the Total Gross Consideration	<u>Total Gross Consideration</u>	<u>Total Gross Consideration</u>	
7	Calculate the Total Net consideration	<u>Total Net Consideration</u>	<u>Total Net Consideration</u>	
8	Calculate WHT as the difference between Total Gross Consideration and Total Net consideration	<u>WHT</u>	<u>WHT</u>	On Deal transaction date, WHT is zero for Taxable security because the Tax will be paid by the client on a future date.

Fixed Deposit

New Placement		
Security:	FD	Note: - Total WHT amount 7083.33 is inclusive of WHT on Trust Fee amount 416.67. So at the time of transaction, client will subtract the WHT on Trust fee amount from Total WHT and pay (7083.33 - 416.67) i.e. 6666.67 upfront as Tax.
Tax Rate	20%	
Value Date	30-Apr-2011	
Issue Date	30-Apr-2011	
Maturity Date	30-May-2011	
Term-Value Date to Maturity	30	
Coupon-Gross	4.2500%	
Seller	IMA03	
Fee Rate	0.2500%	
Rate-Net of Fee, Gross of Tax	4.0000%	
Face Value	1,00,00,000.00	
Gross Int	35,416.67	
WHT	7,083.33	
Net Int	28,333.33	
Maturity Value without Trust fee	1,00,28,333.33	
Trust Fee	2,083.33	
WHT on Trust Fee	416.67	
Net Trust Fee	1,666.67	
Client Maturity Value	1,00,26,666.67	
Pre-Term		
Pre-Term Date	14-May-2011	
Days to go	16.00	
Rate-Net of Fee, Gross of Tax	2.0000%	
Net of Fees	1.7500%	
Days in holding	14	
Face Value	1,00,00,000.00	
Gross Int	7777.77778	
WHT	1555.55556	
Net Int	6222.22222	
Maturity Value without Trust fee	1,00,06,222.22	
Trust Fee	972.2222	
WHT on Trust Fee	194.44	
Net Trust Fee	777.7778	
DST charges	2,191.7800	
Client Maturity Value	1,00,03,252.66	

Special Deposit Account

New Placement	
Security:	BSP SDA
Tax Rate	20%
Value Date	28-Apr-2011
Issue Date	28-Apr-2011
Maturity Date	30-May-2011
Term-Issue to Maturity	32
Term-Value Date to Maturity	32
Coupon-Gross	4.4375%
Seller	IMA03
Fee Rate	0.5000%
Rate-Net of Fee, Gross of Tax	3.9375%
Face Value	70,00,000.00
Gross Int	27,611.11
WHT	5,522.22
Net Int	22,088.89
Maturity Value without Trust fee	70,22,088.89
Trust Fee	3,111.11
WHT on Trust Fee	622.22
Net Trust Fee	2,488.89
Client Maturity Value	70,19,600.00

Pre-Term	
Pre-Term Date	06-May-2011
Days to go	24.00
Rate-Net of Fee, Gross of Tax	2.4375%
Net of Fees	1.9375%
Days in holding	8
Face Value	70,00,000.00
Gross Int	3791.666667
WHT	758.3333333
Net Int	3033.333333
Maturity Value without Trust fee	70,03,033.33
Trust Fee	777.7778
WHT on Trust Fee	155.56
Net Trust Fee	622.2222
Client Maturity Value	70,02,411.11

7. Version History

Version No.	Details	Version Date
1.0	Base Version.	12-01-2016

