



Republic of the Philippines
DEPARTMENT OF FINANCE

Roxas Boulevard Corner Pablo Ocampo, Sr. Street
Manila 1004



DOF Opinion No. 011.2019

ATTY. MALOU P. LIM
Managing Partner (Tax)
Isla Lipana & Co.,
29th Floor, Philamlife Tower,
8767 Paseo de Roxas,
1226 Makati City, Philippines



**SUBJECT: Request for Review of Bureau of Internal Revenue Ruling
No. ITAD 126-14**

Dear **Atty. Lim**:

This refers to the subject letter dated 28 August 2014 ("Request for Review") which you filed with this Department on behalf of LAIII Medical City Cooperatief U.A. ("LMCC U.A.") to request the review of Bureau of Internal Revenue ("BIR") Ruling No. ITAD 126-14 dated 22 July 2014, which ruled that the capital of LMCC U.A. is not divided into shares, contrary to what is being required in the treaty to qualify for the requested 10 percent preferential tax rate, and consequently, subjected the dividends paid by Professional Services, Inc. ("PSI") to LMCC U.A. to the higher preferential tax rate of 15 percent of the gross amount thereof pursuant to Article 10 (2) (b) of the Philippines-Netherlands Tax Treaty.

PSI is a domestic corporation registered with the Securities and Exchange Commission ("SEC") with principal office address at The Medical City, Don Eugenio Lopez Sr. Medical Complex, Ortigas Avenue, Pasig City. It is primarily engaged in establishing, operating, owning a hospital or hospitals, medical and chemical clinics and/or laboratories, and such other enterprise with similar undertaking.

LMCC U.A. is an entity organized under the laws of the Netherlands with registered office address at De Entée 99-197, 1101 HE Amsterdam. LMCC U.A. is engaged in the activities of investing in international market.

LMCC U.A. has no Philippine office and is not registered as a domestic corporation or partnership in the Philippines nor is it licensed to do business in the Philippines.

As stated in the certificate issued by the Corporate Secretary of PSI, LMCC U.A. holds 159,321 shares of common stock representing 18.23% of the total issued and outstanding capital stock of PSI .

On 5 April 2013, the Board of Directors of PSI declared cash dividends in the total amount of Php 150 per share to all stockholders on record as of 31 December 2012.

On 22 July 2014, the BIR issued BIR ITAD Ruling No. 126-14 which provides that since LMCC U.A. is a cooperative, the capital of which is not divided into shares, it does not qualify for the 10% preferential tax rate. Thus, the BIR granted the higher preferential rate of 15%.

It is your claim that all conditions in applying the 10% preferential rate have been satisfied, including the condition that the recipient of the dividends is a company the capital of which is wholly or partly divided into shares.

We agree with your position.

Under the Philippines-Netherlands Tax Treaty, the Philippines may tax the dividends paid by a Philippine company to a resident of the Netherlands at a rate not exceeding (a) 10% of the gross amount of the dividends if the recipient is a company the capital of which is wholly or partly divided into shares and which holds directly at least 10% of the capital of the company paying the dividends; and (b) in all other cases, 15% of the gross amount of dividends. Moreover, to be entitled to the preferential tax rates, the recipient of the dividends who is a resident of the Netherlands must not carry on business in the Philippines pursuant to Article 10 (6) of the same treaty.¹

To avail of the 10% preferential tax rate on the gross amount of the dividends, the recipient company which is a resident in Netherlands must (1) have capital

¹ DGA Ilijan B.V. v. CIR, CTA Case No. 8911, 18 June 2018 *citing* Convention Between the Republic of the Philippines and the Kingdom of the Netherlands ("Philippines-Netherlands Tax Treaty"), Article 10 Par. 2, 1 January 1992.



which is wholly or partly divided into shares and (2) holds directly at least 10% of the capital of the company paying the dividends.

The Philippines-Netherlands Tax Treaty defines company as any body corporate or any other entity which is treated as a body corporate for tax purposes.² However, the same treaty does not have a specific definition for 'shares'. As this is the case, reference can be made to the definition under the Philippine laws as allowed by the same treaty.³

Under the Tax Code of the Philippines, the term 'shares of stock' includes:

“[S]hares of stock of a corporation, warrants and/or options to purchase shares of stock, as well as **units of participation in a partnership** (except general professional partnerships), joint stock companies, joint accounts, joint ventures taxable as corporations, **associations**, and recreation or amusement clubs (such as golf, polo or similar clubs), and mutual fund certificates.”⁴ (emphasis supplied)

The term 'shares of stock' then includes units of participation in associations. And cooperative, under Philippine laws, is considered an association, to wit:

“**A cooperative is an autonomous and duly registered association** of persons, with a common bond of interest, who have voluntarily joined together to achieve their social, economic, and cultural needs and aspirations by making equitable contributions to the capital required, patronizing their products and services and accepting a fair share of the risks and benefits of the undertaking in accordance with universally accepted cooperative principles.”⁵ (emphasis supplied)

Moreover, the OECD Commentary on Article 10 states that in the case of bodies which do not have a capital within the meaning of company law, capital should be taken to mean the total of all contributions to the body which are taken into account for the purpose of distributing profits.⁶

² Philippines-Netherlands Tax Treaty, *Article 3 Par. 1(e)*.

³ 2. As regards the application of the Convention by either of the States, any term not otherwise defined shall, unless the context otherwise requires, have the meaning which it has under the laws of that State relating to the taxes which are the subject of this Convention. (Philippines-Netherlands Tax Treaty, Article 3 Par. 2)

⁴ Tax Reform Act of 1997, Republic Act 8424, as amended, § 22(L) (1 January 1998).

⁵ Philippine Cooperative Code of 2008, Republic Act No. 9520, §1 (Article 3) (17 February 2009).

⁶ [T]he term "capital" is used in relation to the taxation treatment of dividends, i.e., distributions of profits to shareholders. The use of this term in this context implies that, for the purposes of subparagraph (a), it should be used in the sense in which it is used for the purposes of distribution to the shareholder (in particular case, the parent company).



Important to note that LMCC U.A. maintains a capital account for each member and obligations can be imposed from time to time upon each member to contribute capital which shall be credited to their account. Additionally, any amount paid by a member on behalf of LMCC U.A. will be treated as a capital contribution.⁷ Each member shall be entitled to a distribution of net proceeds, if any, on a pro rata basis in accordance with the percentage interest of each member in the capitalization of the cooperative.⁸

Therefore, based on the discussion above, units of participation in cooperatives are considered shares of stock under the Tax Code. It, likewise, follows that the capital of LMCC U.A., as a cooperative, is wholly divided into shares of stock taking into consideration that its capital consists of its members' contributions.

The allegation that LMCC U.A. is a resident of the Netherlands is sufficiently proven by the (1) Authenticated Certificate of Residency issued by the tax authority of Netherlands for LMCC U.A., dated 29 July 2013; and (2) the Certificate of Non-Registration of Company issued by the Securities and Exchange Commission.

LMCC U.A. was also able to comply with the requirement that its capital must be wholly or partly divided into shares. Lastly, to prove that LMCC U.A. is the beneficial owner of 18.23% of the total issued and outstanding capital stock of PSI, it submitted a Secretary's Certificate dated 6 August 2013 showing the shareholdings of LMCC U.A. as well as details of the dividend declaration.

After a careful scrutiny of the records of LMCC U.A. as well as the applicable laws, this Office finds that LMCC U.A. was able to comply with the requirements to be entitled to the 10% preferential tax treaty rate.

xxx xxx xxx

e) In the case of bodies which do not have a capital within the meaning of company law, capital for the purpose of subparagraph (a) is to be taken as meaning the total of all contributions to the body which are taken into account for the purpose of distributing profits. (BIR ITAD Ruling No. 003-15 *citing* OECD Commentary on Article 10, page 189)

⁷ Deed of Incorporation of LMCC U.A., Article 8.

⁸ Deed of Incorporation of LMCC U.A., Article 15.



This ruling is being issued on the basis of the foregoing facts as represented. However, if upon investigation, it will be disclosed that the facts are different, then this ruling shall be considered as null and void.

Thank you.

Sincerely yours,


CARLOS G. DOMINGUEZ
Secretary of Finance
JUN 12 2019

CC **Commissioner Caesar R. Dulay** *Johnes 6/12/19*
Bureau of Internal Revenue

of J.M.
JUN 17 2019

