

2009 BAR EXAMINATIONS

TAXATION

13 September 2009

2 P.M. – 5 P.M.

INSTRUCTIONS

This questionnaire is in TWO (2) PARTS: Part I with ten (10) questions (numbered I to X), contained in six (6) pages; and Part II with ten (10) questions (numbered XI-XX), contained in five (5) pages, for a total number of eleven (11) pages.

Write your answers to Part I and Part II in the corresponding portions indicated in the booklet.

Begin your answer to each numbered question on a separate page; an answer to a subquestion under the same number may be written continuously on the same page and succeeding pages until completed.

Answer the questions directly and concisely. Do not repeat the questions. Write legibly.

HAND IN YOUR NOTEBOOK WITH THIS QUESTIONNAIRE.

GOOD LUCK!

ANTONIO EDUARDO B. NACHURA
CHAIRPERSON
2009 BAR EXAMINATIONS COMMITTEE

PLEASE CHECK THAT THIS SET CONTAINS TWELVE (12) PAGES (INCLUDING THIS PAGE).

WARNING: NOT FOR SALE OR UNAUTHORIZED USE

PART I

I

TRUE or FALSE. Answer TRUE if the statement is true, or FALSE if the statement is false. Explain your answer in not more than two (2) sentences. (5%)

[a] A law that allows taxes to be paid either in cash or in kind is valid.

[b] When the financial position of the taxpayer demonstrates a clear inability to pay the tax, the Commissioner of Internal Revenue may validly compromise the tax liability.

[c] The *doctrine of equitable recoupment* allows a taxpayer whose claim for refund has prescribed to offset tax liabilities with his claim of overpayment.

[d] A law imposing a tax on income of religious institutions derived from the sale of religious articles is valid.

[e] A false return and a fraudulent return are one and the same.

II

Enumerate the four (4) inherent limitations on taxation. Explain each item briefly. (4%)

III

Melissa inherited from her father a 300-square-meter lot. At the time of her father's death on March 14, 1995, the property was valued at ₱720,000.00. On February 28, 1996, to defray the cost of the medical expenses of her sick son, she sold the lot for

₱600,000.00, on cash basis. The prevailing market value of the property at the time of the sale was ₱3,000.00 per square meter.

[a] Is Melissa liable to pay capital gains tax on the transaction? If so, how much and why? If not, why not? (4%)

[b] Is Melissa liable to pay Value Added Tax (VAT) on the sale of the property? If so, how much and why? If not, why not? (4%)

IV

International Technologies, Inc. (ITI) filed a claim for refund for unutilized input VAT with the Court of Tax Appeals (CTA). In the course of the trial, ITI engaged the services of an independent Certified Public Accountant (CPA) who examined the voluminous invoices and receipts of ITI. ITI offered in evidence only the summary prepared by the CPA, without the invoices and the receipts, and then submitted the case for decision.

Can the CTA grant ITI's claim for refund based only on the CPA's summary? Explain. (4%)

V

Jessie brought into the Philippines a foreign-made luxury car, and paid less than the actual taxes and duties due. Due to the discrepancy, the Bureau of Customs instituted seizure proceedings and issued a warrant of seizure and detention. The car, then parked inside a pay parking garage, was seized and brought by government agents to a government impounding facility. The Collector of Customs denied Jessie's request for the withdrawal of the warrant.

Aggrieved, Jessie filed against the Collector a criminal complaint for usurpation of judicial functions on the ground that only a judge may issue a warrant of search and seizure.

[a] Resolve with reasons Jessie's criminal complaint. (4%)

[b] Would your answer be the same if the luxury car was seized while parked inside the garage of Jessie's residence? Why or why not? (4%)

VI

The Sangguniang Bayan of the Municipality of Sampaloc, Quezon, passed an ordinance imposing a storage fee of ten centavos (₱0.10) for every 100 kilos of copra deposited in any bodega within the Municipality's jurisdiction. The Metropolitan Manufacturing Corporation (MMC), with principal office in Makati, is engaged in the manufacture of soap, edible oil, margarine, and other coconut oil-based products. It has a warehouse in Sampaloc, Quezon, used as storage space for the copra purchased in Sampaloc and nearby towns before the same is shipped to Makati. MMC goes to court to challenge the validity of the ordinance, demanding the refund of the storage fees it paid under protest.

Is the ordinance valid? Explain your answer. (4%)

VII

Kenya International Airlines (KIA) is a foreign corporation, organized under the laws of Kenya. It is not licensed to do business in the Philippines. Its commercial airplanes do not operate within Philippine territory, or service passengers embarking from Philippine airports. The firm is represented in the Philippines by its general agent, Philippine Airlines (PAL), a Philippine corporation.

KIA sells airplane tickets through PAL, and these tickets are serviced by KIA airplanes outside the Philippines. The total sales of airline tickets transacted by PAL for KIA in 1997 amounted to

₱2,968,156.00. The Commissioner of Internal Revenue assessed KIA deficiency income taxes at the rate of 35% on its taxable income, finding that KIA's airline ticket sales constituted income derived from sources within the Philippines.

KIA filed a protest on the ground that the ₱2,968,156.00 should be considered as income derived exclusively from sources outside the Philippines since KIA only serviced passengers outside Philippine territory.

Is the position of KIA tenable? Reasons. (4%)

VIII

The City of Manila enacted Ordinance No. 55-66 which imposes a municipal occupation tax on persons practicing various professions in the city. Among those subjected to the occupation tax were lawyers. Atty. Mariano Batas, who has a law office in Manila, pays the ordinance-imposed occupation tax under protest. He goes to court to assail the validity of the ordinance for being discriminatory. Decide with reasons. (3%)

IX

Republic Power Corporation (RPC) is a government-owned and controlled corporation engaged in the supply, generation and transmission of electric power. In 2005, in order to provide electricity to Southern Tagalog provinces, RPC entered into an agreement with Jethro Energy Corporation (JEC), for the lease of JEC's power barges which shall be berthed at the port of Batangas City. The contract provides that JEC shall own the power barges and the fixtures, fittings, machinery, and equipment therein, all of which JEC shall supply at its own cost, and that JEC shall operate, manage and maintain the power barges for the purpose of converting the fuel of RPC into electricity. The contract also stipulates that all real estate taxes and assessments, rates and other

charges, in respect of the power barges, shall be for the account of RPC.

In 2007, JEC received an assessment of real property taxes on the power barges from the Assessor of Batangas City. JEC sought reconsideration of the assessment on the ground that the power barges are exempt from real estate taxes under Section 234 [c] of R.A. 7160 as they are actually, directly and exclusively used by RPC, a government-owned and controlled corporation. Furthermore, even assuming that the power barges are subject to real property tax, RPC should be held liable therefor, in accordance with the terms of the lease agreement. Is the contention of JEC correct? Explain your answer. (4%)

X

ABCD Corporation (ABCD) is a domestic corporation with individual and corporate shareholders who are residents of the United States. For the 2nd quarter of 1983, these U.S.-based individual and corporate stockholders received cash dividends from the corporation. The corresponding withholding tax on dividend income --- 30% for individual and 35% for corporate non-resident stockholders --- was deducted at source and remitted to the BIR.

On May 15, 1984, ABCD filed with the Commissioner of Internal Revenue a formal claim for refund, alleging that under the RP-US Tax Treaty, the deduction withheld at source as tax on dividends earned was fixed at 25% of said income. Thus, ABCD asserted that it overpaid the withholding tax due on the cash dividends given to its non-resident stockholders in the U.S. The Commissioner denied the claim.

On January 17, 1985, ABCD filed a petition with the Court of Tax Appeals (CTA) reiterating its demand for refund.

[a] Does ABCD Corporation have the legal personality to file the refund on behalf of its non-resident stockholders? Why or why not? (3%)

[b] Is the contention of ABCD Corporation correct? Why or why not? (3%)

***** END OF PART I *****

PART II

XI

Raffy and Wena, husband and wife, are both employed by XXX Corporation. After office hours, they jointly manage a coffee shop at the ground floor of their house. The coffee shop is registered in the name of both spouses. Which of the following is the correct way to prepare their income tax return? Write the letter only. DO NOT EXPLAIN YOUR ANSWER. (2%)

[a] Raffy will declare as his income the salaries of both spouses, while Wena will declare the income from the coffee shop.

[b] Wena will declare the combined compensation income of the spouses, and Raffy will declare the income from the coffee shop.

[c] All the income will be declared by Raffy alone, because only one consolidated return is required to be filed by the spouses.

[d] Raffy will declare his own compensation income and Wena will declare hers. The income from the coffee shop shall be equally divided between them. Each spouse shall be taxed separately on their corresponding taxable income to be covered by one consolidated return for the spouses.

[e] Raffy will declare his own compensation income and Wena will declare hers. The income from the coffee shop shall be equally divided between them. Raffy will file one income tax return to cover all the income of both spouses, and the tax is computed on the aggregate taxable income of the spouses.

XII

YYY Corporation engaged the services of the Manananggal Law Firm in 2006 to defend the corporation's title over a property used in the business. For the legal services rendered in 2007, the law firm billed the corporation only in 2008. The corporation duly paid.

YYY Corporation claimed this expense as a deduction from gross income in its 2008 return, because the exact amount of the expense was determined only in 2008. Is YYY's claim of deduction proper? Reasons. (4%)

XIII

In 1999, Xavier purchased from his friend, Yuri, a painting for ₱500,000.00. The fair market value (FMV) of the painting at the time of the purchase was ₱1-million. Yuri paid all the corresponding taxes on the transaction. In 2001, Xavier died. In his last will and testament, Xavier bequeathed the painting, already worth ₱1.5-million, to his only son, Zandro. The will also granted Zandro the power to appoint his wife, Wilma, as successor to the painting in the event of Zandro's death. Zandro died in 2007, and Wilma succeeded to the property.

[a] Should the painting be included in the gross estate of Xavier in 2001 and thus, be subject to estate tax? Explain. (3%)

[b] Should the painting be included in the gross estate of Zandro in 2007 and thus, be subject to estate tax? Explain. (3%)

[c] May a vanishing deduction be allowed in either or both of the estates? Explain. (3%)

XIV

Emiliano Paupahan is engaged in the business of leasing out several residential apartment units he owns. The monthly rental for each unit ranges from ₱8,000.00 to ₱10,000.00. His gross rental income for one year is ₱1,650,000.00. He consults you on whether it is necessary for him to register as a VAT taxpayer. What legal advice will you give him, and why? (4%)

XV

Miguel, a citizen and resident of Mexico, donated US\$1,000.00 worth of stocks in Barack Motors Corporation, a Mexican company, to his legitimate son, Miguelito, who is residing in the Philippines and about to be married to a Filipino girlfriend. Mexico does not impose any transfer tax of whatever nature on all gratuitous transfers of property.

[a] Is Miguel entitled to claim a *dowry exclusion*? Why or why not? (3%)

[b] Is Miguel entitled to the *rule of reciprocity* in order to be exempt from the Philippine donor's tax? Why or why not? (3%)

XVI

Ernesto, a Filipino citizen and a practicing lawyer, filed his income tax return for 2007 claiming optional standard deductions. Realizing that he has enough documents to substantiate his profession-connected expenses, he now plans to file an amended income tax return for 2007, in order to claim itemized deductions, since no audit has been commenced by the BIR on the return he previously filed. Will Ernesto be allowed to amend his return? Why or why not? (4%)

XVII

A final assessment notice was issued by the BIR on June 13, 2000, and received by the taxpayer on June 15, 2000. The taxpayer protested the assessment on July 31, 2000. The protest was initially given due course, but was eventually denied by the Commissioner of Internal Revenue in a decision dated June 15, 2005. The taxpayer then filed a petition for review with the Court of Tax Appeals (CTA), but the CTA dismissed the same.

[a] Is the CTA correct in dismissing the petition for review? Explain your answer. (4%)

[b] Assume that the CTA's decision dismissing the petition for review has become final. May the Commissioner legally enforce collection of the delinquent tax? Explain. (4%)

XVIII

A taxpayer received an assessment notice from the BIR on February 3, 2009. The following day, he filed a protest, in the form of a request for reinvestigation, against the assessment and submitted all relevant documents in support of the protest. On September 11, 2009, the taxpayer, apprehensive because he had not yet received notice of a decision by the Commissioner on his protest, sought your advice.

What remedy or remedies are available to the taxpayer? Explain. (4%)

XIX

Johnny transferred a valuable 10-door commercial apartment to a designated trustee, Miriam, naming in the trust instrument Santino, Johnny's 10-year old son, as the sole beneficiary. The trustee is instructed to distribute the yearly rentals amounting to

₱720,000.00. The trustee consults you if she has to pay the annual income tax on the rentals received from the commercial apartment.

[a] What advice will you give the trustee? Explain. (3%)

[b] Will your advice be the same if the trustee is directed to accumulate the rental income and distribute the same only when the beneficiary reaches the age of majority? Why or why not? (3%)

XX

Masarap Food Corporation (MFC) incurred substantial advertising expenses in order to protect its brand franchise for one of its line products. In its income tax return, MFC included the advertising expense as deduction from gross income, claiming it as an ordinary business expense. Is MFC correct? Explain. (3%)

***** END OF PART II *****

RETURN THIS QUESTIONNAIRE
WITH YOUR BOOKLET