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International Assignment Services

Taxation of International Assignees

Country – Philippines

Human Resources Services

International Assignment Taxation Folio

Table of Contents

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Introduction – International assignees working in Philippines

This booklet is intended to assist foreign nationals sent to work in the Philippines with their tax planning. It gives a broad background to taxation in the Philippines and other important aspects to be considered by a foreign national working in the Philippines on a temporary basis.

This booklet is not intended to be a comprehensive guide. It merely attempts to give an overview of the issues involved. Accordingly, professional advice should be sought before making important decisions.

For additional information on taxation in the Philippines, please see Appendix D.

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Step 1 – Understanding basic principles

The scope of taxation in the Philippines

1. The Philippines taxes aliens, whether or not resident in the Philippines, only on income from sources within the Philippines.

The tax year

2. The tax year runs from January 1st to December 31st.

Methods of calculating tax

3. Income taxes for aliens are levied at the following rates:

   – Progressive rates between 5% and 32% for nonresident aliens engaged in trade or business in the Philippines. For a schedule of the rates of tax please refer to Appendix A;

   – Final flat rate of 25% for nonresident aliens deemed not engaged in trade or business in the Philippines; and

   – Final tax of 15% for alien executives of special entities. For a list of special entities, please refer to the discussion under Taxation of Alien Executives of Special Entities.

Husband and wife

4. For tax purposes, a husband and wife must file one consolidated income tax return, but the tax is computed separately.

Residence - resident aliens

5. A resident alien is an individual who is stateless or is a national of another country and who lives in the Philippines with no definite intention as to length of stay, but who is not a mere transient or sojourner. An expatriate working in the Philippines on a contract for an indefinite period potentially falls into this category.

Residence - nonresident aliens

6. Most expatriates will be classified as nonresident aliens, because their contract will be for a specified period of engagement. A nonresident alien individual who comes to the Philippines and stays there for more than 180 days during any calendar year will be deemed a nonresident alien engaged in trade or business in the Philippines. If the aggregate stay in the Philippines during any calendar year does not exceed 180 days, the individual may be deemed a nonresident alien not engaged in trade or business in the Philippines.

7. Expatriates assigned in the Philippines for a definite period are generally regarded as nonresidents engaged in trade or business in the Philippines.

Step 2 – Understanding the Philippine tax system

Gross income

Employee gross income

8. An alien, whether resident or not, is taxed on compensation income earned from services rendered in the Philippines regardless of where payment is made and whether it is remitted into the Philippines. The nonresident alien is not taxed on compensation income from services performed outside the Philippines. Employee gross income, from the point of view of a nonresident alien engaged in trade or business in the Philippines, includes all payments for services rendered in the Philippines, such as salaries and bonuses, regardless of where payment was made.

9. Philippine social security contributions and union dues paid by employees are not included in gross income and are exempt from taxation.

Fringe benefits tax

10. Fringe benefits furnished to managerial and supervisory-level employees by the employer are subject to a final fringe benefits tax (FBT) of 32% (in general) on the grossed-up monetary value of the benefits. Managerial employees are those who may lay down and execute management policies to hire, transfer, suspend, lay off, recall, discharge, assign, or discipline employees. Supervisory employees are those who effectively recommend such managerial actions if the exercise of authority on behalf of the employer is not merely routine or clerical in nature but requires the use of independent judgment. The FBT is a final tax payable on a calendar quarterly basis by the employer and deductible as part of fringe benefit expense. Benefits subjected to FBT are no longer included in the employees' taxable income.

11. The grossed-up monetary value of a fringe benefit is determined by dividing the actual monetary value of the benefit by 68%. It represents the whole amount of the income realized by the employee, which includes the net amount that has been received plus the amount of fringe benefit tax due from the employee but paid by the employer.

12. The FBT imposed on fringe benefits enjoyed by nonresident aliens not engaged in trade or business within the Philippines is 25% of the grossed-up monetary value of the fringe benefit. The grossed-up monetary value is determined by dividing the actual value of the benefit by 75%.

13. "Fringe benefits" are defined as any goods, services or other benefits furnished or granted in cash or in kind by an employer to an individual employee, except rank and file employees such as, but not limited to, the following:

    – Housing;

    – Expense account;

    – Vehicles of any kind;

    – Salary of household personnel (e.g., maid, driver);

    – Interest on a loan at less than the market rate (currently set at 12%) to the extent of the difference between the market rate and the actual rate granted;

- Membership fees, dues and other expenses borne by the employer for the employee in social and athletic clubs and similar organizations;
- Expenses for foreign travel;
- Holiday and vacation expenses;
- Educational assistance to the employee and dependents; and
- Premiums for life insurance, health and other non-life insurance and similar amounts in excess of what the law allows.

14. The monetary value of benefits in the form of motor vehicles used for both personal and business purposes and housing is equal to 50% of the lease payment or the depreciation value of the property, whichever is applicable. However, if the housing unit is situated in or adjacent (within 50 meters) to the business premises, the benefit is not taxable. Likewise, a motor vehicle used normally for business purposes is not taxable.

15. The following fringe benefits are not taxable:

    - Fringe benefits required by the nature of or necessary to the trade, business or profession or for the convenience or advantage of the employer;
    - Benefits authorized by and exempted from tax under special laws;
    - Employer contributions for the benefit of the employee to retirement, insurance and hospitalization benefit plans;
    - Benefits given to rank and file employees, whether or not granted under a collective bargaining agreement. However, these are subject to withholding tax on compensation, unless otherwise tax exempt; and
    - De minimis (small value) benefits as defined in the rules and regulations.

Valuation of fringe benefits

16. In general, if a fringe benefit is granted in money or directly paid for by the employer, the value of the fringe benefit is the amount granted or paid for. If furnished in property and ownership thereof is transferred to the employee, the value of the fringe benefit is the fair market value of the property as determined by the Commissioner of Internal Revenue, pursuant to his power to prescribe real property values. If the fringe benefit is granted or furnished by the employer in the form of a property but ownership is not transferred to the employee, the value of the fringe benefit is equal to the depreciation value of the property.

Taxation of alien executives of special entities

17. Expatriates employed by special entities or industries enjoy certain tax concessions. These include alien executives of offshore banking units, service contractors and subcontractors engaged in oil exploration activities, and regional headquarters and regional operating headquarters of multinational companies. They are taxed at 15% on their gross compensation income. The applicable FBT rate is also 15%. The grossed-up monetary value is determined by dividing the actual value of the benefit by 85%.

Capital gains and investment income

18. Nonresident aliens are taxed on Philippine-source capital gains, irrespective of their period of stay in the Philippines. The rates are 0.5% of the gross sales for those shares of stocks listed and traded in the stock exchange; 5% on the first PHP100,000 and 10% on the excess of the net capital gains for unlisted shares of stock; and 6% of the higher of the gross sales price or fair market value of real property sold, withheld at the time of sale. Capital losses are deductible only from capital gains. In computing net capital gains or losses

from other capital assets, only 50% of the gain or loss is to be taken into account if the capital asset has been held for more than 12 months; otherwise, 100% of the gain or loss is to be considered. Any unused capital losses (in an amount not in excess of the net income for such year) may be carried forward to the succeeding taxable year and treated as a loss from the sale or exchange of a capital asset held for less than 12 months.

19. A nonresident alien is also taxed on Philippine-source investment income such as interest, dividends and royalties at the rate of 20% (for those engaged in trade or business in the Philippines) or 25% (for those not engaged in trade or business in the Philippines), or a lower treaty rate. The tax is final and is withheld at source, and the income is no longer subject to the graduated rates.

20. Resident aliens are taxed on their Philippine-source income at graduated rates. However, Philippine-source interest and royalties are taxed at 20%. Interest on residents' deposits under the expanded foreign currency deposit system (FCDU) accounts is taxed at 7.5%, while interest on long-term deposits or investment in the form of savings, common or individual trust funds and other investments evidenced by certificates, and so on, is exempt from tax, subject to certain conditions. Interest income on FCDU accounts of nonresidents is tax exempt. Royalties on literary works and musical compositions are subject to a final tax of 10%. Dividend income received from a domestic corporation is taxed at 10%.Tax rates for capital gains from shares of stock and real property are the same as those for nonresident aliens.

Deductions

Business deductions

21. Aliens, whether residents or not, who are receiving only salary or compensation income are not allowed any deduction against such income.

22. In the case of individuals engaged in business or the practice of a profession, the following expenses are allowed as deductions from gross income:

- All ordinary and necessary expenses paid or incurred during the taxable year in connection with the trade, business or profession, including raw materials, supplies and direct labor;
- Wages and other forms of compensation for personal services actually rendered, including the grossed-up monetary value of fringe benefits and travel expenses incurred in the pursuit of the trade or profession;
- Business rentals;
- Interest paid or incurred within a taxable year in connection with the conduct of a taxpayer's profession, trade or business, less an amount equal to a certain percentage of the interest income subject to final tax;
- Entertainment, amusement and recreation expenses, not to exceed the following ceilings:
  - 0.50% of net sales for taxpayers engaged in sale of goods or properties; or
  - 1% of net revenue for taxpayers engaged in sale of services, including professionals and leaser of properties.
- Taxes;
- Losses;
- Bad debts;
- Depreciation;
- Charitable and other contributions, subject to certain limitations; and
- Research and development expenditures.

23. In lieu of these allowable deductions, an individual other than a nonresident alien may elect a standard deduction not exceeding 40% of gross income.

Nonbusiness expenses

24. Home mortgage interest, medical expenses, contributions, and other personal expenses cannot be claimed as deductions for income tax purposes. However, Philippine social security contributions are excluded from gross income.

Personal allowances

25. Resident aliens and, subject to certain conditions, nonresident aliens engaged in trade or business in the Philippines, are allowed a personal exemption of PHP50,000. An additional exemption of PHP25,000 for each dependent child (not to exceed four dependents) is allowed to married individuals. These personal and additional exemptions take the form of deductions instead of tax credits.

26. A family with gross income of not more than PHP250,000 for the year may deduct premium payments for health/hospitalization insurance up to a maximum of PHP2,400.

Tax credits

27. Aliens deriving income from foreign sources are not allowed a tax credit for foreign income taxes against Philippine income tax.

Other taxes

Social security taxes

28. The maximum annual social security and health benefit contribution payable by an individual taxpayer for 2011 is PHP11,700. Social taxes consist of contributions to the Social Security System (SSS), Philippine Health Insurance Corporation (Philhealth) and Home Development Mutual Fund (HDMF).

Value-added tax (VAT)

29. A 12% value added tax (VAT) is imposed on services performed by entertainers, musical, radio, movie, and television and stage directors; and professional athletes; services rendered by customs, real estate, stock, immigration, and commercial brokers; and services performed in the exercise or practice of profession or calling, except professional services rendered by general professional partnerships. The VAT is based on the gross receipts representing the contract price, compensation, service fee, rental, or royalty, including the amount charged for materials supplied with the services and deposits and advanced payments actually or constructively received during the taxable period/quarter for the services performed or to be performed for another person, excluding VAT.

Local taxes on income

30. The local governments are not authorized to impose any tax on income.

Individuals are, however, subject to a community tax if they have been employed for a consecutive period of at least 30 days during the tax year, are engaged in business, own real property in the Philippines or are required to fill out an income tax return. The community tax varies between PHP 5 up to a maximum of PHP 5,005, depending on the income of the taxpayer.

Tax administration
Returns

31. For tax purposes, a husband and wife must file one consolidated income tax return, but the tax is computed separately. Income that cannot be definitely attributed or identified as exclusive income of either spouse is divided equally between them. Generally, this results in lower combined tax liability than when the tax is jointly computed.

32. Substituted filing of returns is mandatory for all qualified employees. Substituted filing is applicable when the employer's annual return of withholding tax on compensation and final tax (BIR Form 1604CF) may be considered as the "substitute" income tax return of its employees inasmuch as the information provided in his or her Certificate of Income Tax Withheld (BIR Form 2316) would exactly be the same information contained in Form 1604CF.

33. Substituted filing, however, will not apply to nonresident aliens engaged in trade or business in the Philippines. All individual taxpayers who do not qualify for substituted filing are required to file their returns on a calendar-year basis. The return must be filed on or before April 15th of the succeeding year.

Payment of tax

34. Generally, the income tax withheld from the salaries or compensation of aliens, resident or not, is equal to their final tax liability on such compensation. If not, the balance must be paid at the time the return is filed. In certain cases, income tax liability may be paid in two equal installments.

Business income

35. For an individual, whether citizen or resident alien, who is self-employed or practices a profession, the tax rates are the same as above. An individual with a taxable compensation income of US$25,000 and a taxable business or professional income of US$25,000 will have a total taxable income of US$50,000 (PHP2,215,550) and will pay a total individual income tax of US$15,210 (PHP673,976).

36. In the case of nonresident aliens not doing business in the Philippines, the tax rate is a flat 25% of the gross income received from all sources within the Philippines.

Income subject to final tax

37. This is usually on passive investment income. For resident and nonresident aliens engaged in trade or business in the Philippines, the maximum rate is 20%; for nonresident aliens not engaged in trade or business in the Philippines, the rate is a flat 25%. (See also discussions under "Capital gains and investment income").

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Appendix A – Individual income tax rates for 2011

Tax rates

Rates of tax on income of aliens, resident or not, depend on the nature of their income—i.e., compensation income, income subject to final tax or other income (see below).

Compensation

For resident aliens and nonresident aliens doing business (as earlier defined) and receiving compensation income, the tax rates are as follows (denominated in PHP):

Taxable income over	Not over	Tax on Column 1	Percentage on excess
0	10,000	–	5%
10,000	30,000	500	10%
30,000	70,000	2,500	15%
70,000	140,000	8,500	20%
140,000	250,000	22,500	25%
250,000	500,000	50,000	30%
500,000	and above	125,000	32%

For example, the tax due on a taxable compensation income of US$25,000 (PHP1,107,775) is US$7,210 (PHP319,488).

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Appendix B – Typical tax computation

Typical tax computation for 2011

Assumptions

- Resident alien husband and wife with two dependent children;
- Salary and allowances of husband arising from employment: salary of PHP652,000; living allowances of PHP100,000; housing benefits (100%) of PHP300,000;
- Teaching salary of wife: PHP68,000;
- Gross dividend income from investment in shares of stock of a domestic corporation of PHP10,000;
- Interest of PHP20,000 on peso bank account;
- Capital gain on sale of shares of PHP5,000; and
- Taxes withheld by employer of husband at PHP173,640 and by employer of wife at PHP1,300.

Tax computation (PHP)	Husband	Wife
Gross income (1):		
Salary	652,000	68,000
Living allowances	100,000	
Housing benefits (300,000) (2)		
Total income	**752,000**	**68,000**
Deductions:		
Personal exemption	(50,000)	(50,000)
Additional exemption for dependent children (3)	(50,000)	
Total deductions	**(100,000)**	**(50,000)**
Net taxable income	**652,000**	**18,000**
Tax due:		
On first 500,000	125,000	
On remainder of 152,000 at 32%	48,640	
On first 10,000		500
On remainder of 8,000 at 10%		800
Total tax	**173,640**	**1,300**
Less—Tax withheld by employer per Form 2316 (4)	(173,640)	(1,300)
Net tax due	***0***	***0***

Notes

The following items were not included in the income tax return because they are subject to final tax:

Interest on peso bank account	20,000
Capital gain on sale of shares	5,000
Dividend income	10,000
Housing benefit	300,000

1. A final tax of 10% applies to dividend income.

2. Housing benefits are subject to FBT, payable by the employer. Under the fringe benefits tax regulations, such benefits are taxable to the extent of 50% of the rentals for the house or living quarters used by the employee and paid by the employer if the lease contract is in the name of the employer.

   To compute the fringe benefits tax due, 50% of the rental payment is grossed-up before applying the 32% tax. Thus, the grossed-up value of PHP150,000 is PHP220,588, and the tax payable is PHP70,588.

3. The additional exemption for dependent children is to be claimed by the husband unless he explicitly waives his right in favor of his wife.

4. For individuals receiving salary and other allowances from one employer only, the tax due is usually equal to tax withheld, since the employer is required to compute and withhold the total tax due on the employee's compensation earned during the year, using the annual graduated income tax table, before paying the last payroll for the year.

5. Philippine social tax contributions, if any, made by the resident alien and/or his wife to the Philippine social security agencies shall be allowed as deductions from gross income in calculating their tax liabilities for the year.

6. The above individual tax calculation also applies to nonresident aliens engaged in trade or business in the Philippines for their Philippine-source income, except that personal exemptions are allowed only under certain conditions.

7. Exchange rate of the Philippine peso as of February 1, 2011: US$1 = PHP44.311.

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Appendix C – Double-taxation agreements

Countries with which the Philippines currently has double-taxation agreements (other than for shipping and air transport only):

Australia	Germany	Pakistan
Austria	Hungary	Romania
Bahrain	India	Russia
Bangladesh	Indonesia	Singapore
Belgium	Israel	Spain
Brazil	Italy	Sweden
Canada	Japan	Switzerland
China	Korea	Thailand
Czech	Malaysia	United Kingdom of Great Britain and Northern Ireland
Denmark	Netherlands	United States of America
Finland	New Zealand	Vietnam
France	Norway	

Last Updated: February 2011

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Appendix D – Philippines contacts and offices

Contacts

Myrna M. Fernando
Tel: (63) (2) 845 2728, (63) (2) 459 2003 (direct)
Fax: (63) (2) 845 2806
Email: myrna.fernando@ph.pwc.com

Offices

Cebu City	Manila
Isla Lipana & Co. (a PwC member firm) Unit 306 Keppel Center Samar Loop corner Cardinal Rosales Ave Cebu Business Park Cebu City 6000 Philippines Mail Address: PO Box 715 Cebu City Philippines Tel: [63] (32) 231 6464, (32) 233 5020, (32) 231 5022 Fax: [63] (32) 233 9615	Isla Lipana & Co. (a PwC member firm) 29th Floor Philamlife Tower 8767 Paseo de Roxas Makati City 1226 Philippines Mail Address: PO Box 2288 Manila 1099 Philippines Tel: [63] (2) 845 2728 Fax: [63] (2) 845 2806

Last Updated: February 2011

Menu

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