

ADVISORY ON TAXATION OF CROSS-BORDER SERVICES

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Further Clarifying the Tax Treatment of
Cross-Border Services in Light of the
Supreme Court *En Banc* Decision on *Aces
Philippines Cellular Satellite Corp. v.
Commissioner of Internal Revenue, G.R. No.
226680, August 30, 2022*

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**Clarifying the Tax Treatment of Cross-Border Services
in Light of the Supreme Court *En Banc* Decision on
Aces Philippines Cellular Satellite Corp. v. Commissioner of Internal Revenue,
*G.R. No. 226680, August 30, 2022***

Background of the *Aces Case*

The *Aces Case* involves the tax treatment of final withholding tax (FWT) on income payments to non-resident foreign corporations. In this case, the income payments were made for satellite airtime services rendered by Aces Bermuda to Aces Philippines.

The Supreme Court held that the determination of the tax treatment (*i.e.* whether or not the satellite airtime fee payments are subject to FWT) requires a two-tiered approach:

Two-Tiered Approach		Rationale
1	Source of the income	Satellite airtime fees accrue only when the satellite airtime is delivered to Aces Philippines and is utilized by the Philippine subscriber for a voice or data call
2	Situs of the source	Ace Bermuda's service is considered as completed and performed in the Philippines because: <ul style="list-style-type: none">☑ The income-generating activity is directly associated with the gateways located within the Philippine territory; and☑ Engaging in the business of providing satellite communication services in the Philippines is a government regulated industry.

Cross-Border Services Akin to that of *Aces v. CIR*

International service provision (or cross-border services) includes the following or similar transactions:

- | | |
|-----------------------|--------------------------------|
| ☑ Consulting Services | ☑ Engineering and Construction |
| ☑ IT Outsourcing | ☑ Education and Training |
| ☑ Financial Services | ☑ Tourism and Hospitality |
| ☑ Telecommunications | ☑ Other Similar Services |

Taxation of Cross-Border Services

Income Tax: If the income-generating activities in the Philippines are **deemed essential**, the income derived from these activities would be considered as sourced from the Philippines. It is thus subject to income tax and FWT.

It is imperative to ascertain whether the particular stages occurring in the Philippines are so integral to the overall transaction that the business activity would not have been accomplished without them.

Value-Added Tax: If the service provider is outside the country but the service is **utilized, applied, executed, or consumed for a recipient within the Philippines**, VAT is applicable. Consequently, payment for such service shall be subject to final withholding VAT.

Treatment of Reimbursable/Allocable Expenses Between Related Parties

Rule: The reduction of expenses for a foreign corporation can be **considered as income** because it increases the foreign corporation's net income or profit.

Also, reimbursable/allocable expenses charged by a foreign corporation should contribute to the value/benefit received by a local company.

Cross-Border Transactions with No Benefits Derived by the Philippine Company

Rule: It may be seen as an **attempt to evade taxes or manipulate profits**.

It follows the *"source-based taxation principle"* or that the source of income should be determined by the location of the business activity that generates the income, rather than the location of the payout or where it is physically received.

Source:

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