Republic of the Philippines
Supreme Court
Manila

EN BANC

BANCO DE ORO, BANK OF COMMERCE, CHINA BANKING CORPORATION, METROPOLITAN BANK & TRUST COMPANY, PHILIPPINE BANK OF COMMUNICATIONS, PHILIPPINE NATIONAL BANK, PHILIPPINE VETERANS BANK AND PLANTERS DEVELOPMENT BANK, Petitioners, **RIZAL COMMERCIAL BANKING CORPORATION AND RCBC CAPITAL CORPORATION**, Petitioners-Intervenors, **CAUCUS OF DEVELOPMENT NGO NETWORKS**, Petitioner-Intervenor, -versus- **REPUBLIC OF THE PHILIPPINES, THE COMMISSIONER OF INTERNAL REVENUE, BUREAU OF**	**G.R. No. 198756** Present: SERENO, *C.J.*, CARPIO, VELASCO, JR., LEONARDO-DE CASTRO, BRION,* PERALTA, BERSAMIN, DEL CASTILLO, VILLARAMA, JR., PEREZ, MENDOZA, REYES, PERLAS-BERNABE, LEONEN, and JARDELEZA, *JJ.*

* On leave.

INTERNAL REVENUE, SECRETARY OF FINANCE, DEPARTMENT OF FINANCE, THE NATIONAL TREASURER AND BUREAU OF TREASURY,
Respondents.

Promulgated:
JANUARY 13, 2015

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DECISION

LEONEN, *J.*:

The case involves the proper tax treatment of the discount or interest income arising from the ₱35 billion worth of 10-year zero-coupon treasury bonds issued by the Bureau of Treasury on October 18, 2001 (denominated as the Poverty Eradication and Alleviation Certificates or the PEACe Bonds by the Caucus of Development NGO Networks).

On October 7, 2011, the Commissioner of Internal Revenue issued **BIR Ruling No. 370-2011**[1] (2011 BIR Ruling), declaring that the PEACe Bonds being deposit substitutes are subject to the 20% final withholding tax. Pursuant to this ruling, the Secretary of Finance directed the Bureau of Treasury to withhold a 20% final tax from the face value of the PEACe Bonds upon their payment at maturity on October 18, 2011.

This is a petition for certiorari, prohibition and/or mandamus[2] filed by petitioners under Rule 65 of the Rules of Court seeking to:

> a. ANNUL Respondent BIR's Ruling No. 370-2011 dated 7 October 2011 [and] other related rulings issued by BIR of similar tenor and import, for being unconstitutional and for having been issued without jurisdiction or with grave abuse of discretion amounting to lack or excess of jurisdiction. . .;
>
> b. PROHIBIT Respondents, particularly the BTr, from withholding or collecting the 20% FWT from the payment of the face value of the Government Bonds upon their maturity;
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> c. COMMAND Respondents, particularly the BTr, to pay the full amount of the face value of the Government Bonds upon maturity. . .; and
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> d. SECURE a temporary restraining order (TRO), and subsequently a writ of preliminary injunction, enjoining Respondents, particularly the BIR and the BTr, from withholding or collecting 20% FWT on the Government Bonds and the respondent BIR from enforcing

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1 *Rollo*, pp. 217–230.
2 Id. at 13–83.

> the assailed 2011 BIR Ruling, as well as other related rulings issued by the BIR of similar tenor and import, pending the resolution by [the court] of the merits of [the] Petition.[3]

Factual background

By letter[4] dated March 23, 2001, the Caucus of Development NGO Networks (CODE-NGO) "with the assistance of its financial advisors, Rizal Commercial Banking Corp. ("**RCBC**"), RCBC Capital Corp. ("**RCBC Capital**"), CAPEX Finance and Investment Corp. ("**CAPEX**") and SEED Capital Ventures, Inc. (**SEED**),"[5] requested an approval from the Department of Finance for the issuance by the Bureau of Treasury of 10-year zero-coupon Treasury Certificates (T-notes).[6] The T-notes would initially be purchased by a special purpose vehicle on behalf of CODE-NGO, repackaged and sold at a premium to investors as the PEACe Bonds.[7] The net proceeds from the sale of the Bonds "will be used to endow a permanent fund (Hanapbuhay® Fund) to finance meritorious activities and projects of accredited non-government organizations (NGOs) throughout the country."[8]

Prior to and around the time of the proposal of CODE-NGO, other proposals for the issuance of zero-coupon bonds were also presented by banks and financial institutions, such as First Metro Investment Corporation (proposal dated March 1, 2001),[9] International Exchange Bank (proposal dated July 27, 2000),[10] Security Bank Corporation and SB Capital Investment Corporation (proposal dated July 25, 2001),[11] and ATR-Kim Eng Fixed Income, Inc. (proposal dated August 25, 1999).[12] "[B]oth the proposals of First Metro Investment Corp. and ATR-Kim Eng Fixed Income indicate that the interest income or discount earned on the proposed zero-coupon bonds would be subject to the prevailing withholding tax."[13]

A **zero-coupon bond** is a bond bought at a price substantially lower than its face value (or at a deep discount), with the face value repaid at the time of maturity.[14] It does not make periodic interest payments, or have so-called "coupons," hence the term zero-coupon bond.[15] However, the discount to face value constitutes the return to the bondholder.[16]

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3 Id. at 16–17.
4 Id. at 419–421.
5 Id. at 279.
6 Id. at 419.
7 Id.
8 Id.
9 Id. at 423–439.
10 Id. at 440–451.
11 Id. at 452–461.
12 Id. at 462–468.
13 Id. at 281.
14 Frank J. Fabozzi with Steven V. Mann, THE HANDBOOK OF FIXED INCOME SECURITIES 310-311 (7th ed., 2005).
15 Id.
16 Id.

On May 31, 2001, the Bureau of Internal Revenue, in reply to CODE-NGO's letters dated May 10, 15, and 25, 2001, issued BIR Ruling No. 020-2001[17] on the tax treatment of the proposed PEACe Bonds. BIR Ruling No. 020-2001, signed by then Commissioner of Internal Revenue René G. Bañez confirmed that the PEACe Bonds would not be classified as deposit substitutes and would not be subject to the corresponding withholding tax:

> Thus, to be classified as "deposit substitutes", the borrowing of funds must be obtained from twenty (20) or more individuals or corporate lenders at any one time. *In the light of your representation that the PEACe Bonds will be issued only to one entity, i.e., Code NGO, the same shall not be considered as "deposit substitutes" falling within the purview of the above definition. Hence, the withholding tax on deposit substitutes will not apply.*[18] (Emphasis supplied)

The tax treatment of the proposed PEACe Bonds in BIR Ruling No. 020-2001 was subsequently reiterated in BIR Ruling No. 035-2001[19] dated August 16, 2001 and BIR Ruling No. DA-175-01[20] dated September 29, 2001 (collectively, the 2001 Rulings). In sum, these rulings pronounced that to be able to determine whether the financial assets, i.e., debt instruments and securities are deposit substitutes, the "20 or more individual or corporate lenders" rule must apply. Moreover, the determination of the phrase "at any one time" for purposes of determining the "20 or more lenders" is to be determined at the time of the original issuance. Such being the case, the PEACe Bonds were not to be treated as deposit substitutes.

Meanwhile, in the memorandum[21] dated July 4, 2001, Former Treasurer Eduardo Sergio G. Edeza (Former Treasurer Edeza) questioned the propriety of issuing the bonds directly to a special purpose vehicle considering that the latter was not a Government Securities Eligible Dealer (GSED).[22] Former Treasurer Edeza recommended that the issuance of the Bonds "be done through the ADAPS"[23] and that CODE-NGO "should get a GSED to bid in [sic] its behalf."[24]

Subsequently, in the notice to all GSEDs entitled Public Offering of Treasury Bonds[25] (Public Offering) dated October 9, 2001, the Bureau of Treasury announced that "□30.0B worth of 10-year Zero[-] Coupon Bonds

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17 *Rollo*, pp. 133–137.
18 Id. at 136.
19 Id. at 138–140.
20 Id. at 141–143.
21 Id. at 473–474.
22 Id.
23 Id. at 474. ADAPS is short for Automated Debt Auction Processing System as per DOF Department Order 141-95.
24 Id.
25 Id. at 130.

[would] be auctioned on October 16, 2001[.]"[26] The notice stated that the Bonds "shall be issued to not more than 19 buyers/lenders hence, the necessity of a manual auction for this maiden issue."[27] It also required the GSEDs to submit their bids not later than 12 noon on auction date and to disclose in their bid submissions the names of the institutions bidding through them to ensure strict compliance with the 19 lender limit.[28] Lastly, it stated that "the issue being limited to 19 lenders and while taxable shall not be subject to the 20% final withholding [tax]."[29]

On October 12, 2001, the Bureau of Treasury released a memo[30] on the "Formula for the Zero-Coupon Bond." The memo stated in part that the formula (in determining the purchase price and settlement amount) "is only applicable to the zeroes that are not subject to the 20% final withholding due to the 19 buyer/lender limit."[31]

A day before the auction date or on October 15, 2001, the Bureau of Treasury issued the "Auction Guidelines for the 10-year Zero-Coupon Treasury Bond to be Issued on October 16, 2001" (Auction Guidelines).[32] The Auction Guidelines reiterated that the Bonds to be auctioned are "[n]ot subject to 20% withholding tax as the issue will be limited to a maximum of 19 lenders in the primary market (pursuant to BIR Revenue Regulation No. 020 2001)."[33] The Auction Guidelines, for the first time, also stated that the

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26 Id.
27 Id.
28 Id.
29 Id.
30 Id. at 131. The memo states:

Below is the formula in determining the purchase price and settlement amount of the P30B Zero-Coupon Bond to be auctioned on October 16, 2001. Please be advised that this is only applicable to the zeroes that are not subject to the 20% final withholding due to the 19 buyer/lender limit.

1. SA = PP * FV
2. $PP = 1/[1 + i/m]^n$

$n = (MP * m) – E/x$
$x = 360/m$
E = Settlement Date – Original Issue Date
(Y2 – Y1) 360 + (M2 – M1) 30 + (D2 – D1)
Where:
Y2 M2 D2 = Settlement Date/Value Date
Y1 M1 D1 = Original Issue Date
Note:
a) Based on 30/360 days count, compounded semi-annually
b) If D1 [=]– 31 change it to 30
c) Up to at least 10 decimal places

Where:
SA = Settlement Amount → Cash Out
PP = Purchase Price
FV = Face Value
i = Yield to Maturity
x = days in the present compounding period
m = no. of conversion per year
(1 = annual, 2 = semi-annual, 4 = quarterly)
MP = Maturity Period (or tenor) in years
E = Bond Lapsed Days

31 Id.
32 Id. at 132.
33 Id.

Bonds are "[e]ligible as liquidity reserves (pursuant to MB Resolution No. 1545 dated 27 September 2001)[.]"[34]

On October 16, 2001, the Bureau of Treasury held an auction for the 10-year zero-coupon bonds.[35] Also on the same date, the Bureau of Treasury issued another memorandum[36] quoting excerpts of the ruling issued by the Bureau of Internal Revenue concerning the Bonds' exemption from 20% final withholding tax and the opinion of the Monetary Board on reserve eligibility.[37]

During the auction, there were 45 bids from 15 GSEDs.[38] The bidding range was very wide, from as low as 12.248% to as high as 18.000%.[39]

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34 Id.

35 Id. at 292.

36 Id. at 494.

37 Id. at 292.

38 Id.

39 Id. at 496–497. *See* Milo Tanchuling, *No peace in PEACE bonds,* INQUIRER, October 22, 2011 <http://opinion.inquirer.net/15839/no-peace-in-peace-bonds#ixzz3O1mBfUD8> (visited January 6, 2015): "Financial analysts said the PEACe bonds hold the record for having the widest differential between the highest bid and the lowest bid. This is an indication of an information asymmetry in the market. When the latter exists during an auction, the auction must be declared a failure.";
See also David Grimes, *Revisiting the Peace Bonds,* October 7, 2011 <http://systemisbroken.blogspot.com/2011/10/revisiting-peace-bonds.html> (visited January 6, 2015): "The bid differential of 5.752% between the top winning bid and the bottom losing bid stands out as one of the highest ever in the history of 10 year Philippine Treasury Bond auctions (65 auctions since 1998 to 2011). No other auction prior to the PEACe Bond auction on October 16, 2001 or after the PEACe Bond auction has ever come close.

In fact, the high low differential in auctions of 10 year Philippine Treasury Bonds from 1998 to 2001 (prior to the PEACe Bond auction on October 16, 2001) was a marginal 0.422%. In other words, the PEACe Bonds differential was over ten times the historical average. . . .

. . . .

The Bureau of Treasury has held no less than 8 auctions of zero-coupon bonds since the PEACe Bond offering in 2001. . . . The bid differentials for these subsequent zero-coupon bond auctions from 2004 to 2006 averaged 0.601% and ranged from as low as 0.250% to as high as 1.480%.

. . . .

[B]ased on the documents furnished by CODE-NGO, the GSEDs knew:

1. Only one week in advance that the auction of the zero-coupon bond issue was pushing through; and
2. Only one day before the auction date, the issue's terms, conditions, and eligibilities that would define its marketability, price, and target market, as well as the bidding procedure to be used.

In short, the GSEDs had only one day to understand this very new and innovative financial instrument. They had only one day to test its marketability with potential buyers who have the means to place a minimum bid of at least PHP 500.0 million face value or PHP 150.0 million cash value. They had only one day to price it and submit a winning bid.

. . . .

On the other hand, CODE-NGO and RCBC, because they had been working on this flotation since March 2001, knew all the details surrounding the auction even before it was announced to the other bidders. They were extremely prepared and fully armed information-wise. No wonder that CODE-NGO/RCBC won the entire auction."
See also Freedom from Debt Coalition, *Annex 1: Anatomy of the PEACe Bonds controversy,* January 30, 2002 <http://www.fil-globalfellows.org/anatomybonds.html> (visited January 6, 2015):"**Information Gaps**

Treasurer Edeza made sure to brief members of the Investment House Association of the Philippines about the bond issue, at one of their regular meetings several weeks before the auction. Nevertheless we observe gaps in the official notices of the government regarding this flotation and the auction.

For one, even though this was a maiden issue of a zero-coupon bond of the Republic of the Philippines, neither a prospectus nor a tombstone was prepared and issued. . . .

The first written notice of the Treasury to the GSEDs was dated 09 October 2001, a week before the auction. This memo made no mention of secondary reserve eligibility. It said only that the bond

Nonetheless, the Bureau of Treasury accepted the auction results.[40] The cut-off was at 12.75%.[41]

After the auction, RCBC which participated on behalf of CODE-NGO was declared as the winning bidder having tendered the lowest bids.[42] Accordingly, on October 18, 2001, the Bureau of Treasury issued ₱35 billion worth of Bonds at yield-to-maturity of 12.75% to RCBC for approximately ₱10.17 billion,[43] resulting in a discount of approximately ₱24.83 billion.

Also on October 16, 2001, RCBC Capital entered into an underwriting agreement[44] with CODE-NGO, whereby RCBC Capital was appointed as the Issue Manager and Lead Underwriter for the offering of the PEACe Bonds.[45] RCBC Capital agreed to underwrite[46] on a firm basis the offering, distribution and sale of the ₱35 billion Bonds at the price of ₱11,995,513,716.51.[47] In Section 7(r) of the underwriting agreement, CODE-NGO represented that "[a]ll income derived from the Bonds, inclusive of premium on redemption and gains on the trading of the same, are exempt from all forms of taxation as confirmed by Bureau of Internal Revenue (BIR) letter rulings dated 31 May 2001 and 16 August 2001,

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issue was limited to the 19-lender rule and therefore was exempted from the 20 percent withholding tax. . . .

The secondary reserve eligibility was finally mentioned in the Treasury Notice that was released on 15 October 2001, one day before the auction.

On the day of the auction the Treasury gave further clarification on the tax exemption and secondary reserve eligibility features of the PEACe Bonds.

We do not know what time this memo was released to the dealers, considering that the cutoff time for submitting bids was 12 noon. But this memo is also an indication that until the day of the auction itself, RCBC's rival bidders needed further clarification on crucial aspects of the PEACe Bond float that should have been factored into their bids.

No mention at all was made of Insurance Commission eligibility, or that winning bidders could apply to Insurance Commission for eligibility.

Based on this information, we surmise that the GSEDs had far less time than CODE-NGO/RCBC to look for investors, price the bonds accordingly and submit a winning bid. On the other hand, because CODE-NGO and RCBC had worked on this flotation since the beginning and knew all the details surrounding the auction before it was announced to the bidders, they were extremely prepared to bid appropriately. They also had a seven-month headstart over their rival bidders, to mobilize the PhP10 billion of resources — whose nature has yet to be determined — needed to snag the entire auction. Between a bank that had seven months to accumulate several billions of pesos and others that had only a week's notice — the cost of capital of the latter would be significantly much higher. This cost of quickly liquefying assets contributed to the costs of and the consequent weaker ability of the other banks to bid aggressively even if they intended to.

. . . .

If the auction were a 'level playing field' where GSEDs have the same competencies and access to the same information, the chances of RCBC winning all its four bids is 24 in 3,575,880 (0.0007 percent). Despite such odds RCBC won all its four bids. This means that RCBC operated on either a tremendous advantage, or on a dire need far greater than its competitors, or both."

40 *Rollo*, p. 292.

41 Id.

42 Id. at 27.

43 Id. at 27 and 497.

44 Id. at 1060–1074.

45 Id. at 1060.

46 Id. at 1066. Section 5 of the underwriting agreement provides that the "underwriting fee and selling commission [shall be] in such amount as may be agreed upon between CODE NGO and [RCBC Capital] but not to exceed two percent (2%) of the total issue price of the total Bonds sold[.]"

47 Id. at 1062.

respectively."[48]

RCBC Capital sold the Government Bonds in the secondary market for an issue price of □11,995,513,716.51. Petitioners purchased the PEACe Bonds on different dates.[49]

BIR rulings

On October 7, 2011, "the BIR issued the assailed 2011 BIR Ruling imposing a 20% FWT on the Government Bonds and directing the BTr to withhold said final tax at the maturity thereof, [allegedly without] consultation with Petitioners as bondholders, and without conducting any hearing."[50]

"It appears that the assailed 2011 BIR Ruling was issued in response to a query of the Secretary of Finance on the proper tax treatment of the discount or interest income derived from the Government Bonds."[51] The Bureau of Internal Revenue, citing three (3) of its rulings rendered in 2004 and 2005, namely: BIR Ruling No. 007-04[52] dated July 16, 2004; BIR Ruling No. DA-491-04[53] dated September 13, 2004; and BIR Ruling No. 008-05[54] dated July 28, 2005, declared the following:

> The Php 24.3 billion discount on the issuance of the PEACe Bonds should be subject to 20% Final Tax on interest income from deposit substitutes. It is now settled that all treasury bonds (including PEACe Bonds), regardless of the number of purchasers/lenders at the time of origination/issuance are considered deposit substitutes. In the case of zero-coupon bonds, the discount (i.e. difference between face value and purchase price/discounted value of the bond) is treated as interest income of the purchaser/holder. Thus, the Php 24.3 interest income should have been properly subject to the 20% Final Tax as provided in Section 27(D)(1) of the Tax Code of 1997. . . .
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> . . . .
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> However, at the time of the issuance of the PEACe Bonds in 2001, the BTr was not able to collect the final tax on the discount/interest income realized by RCBC as a result of the 2001 Rulings. Subsequently, the issuance of BIR Ruling No. 007-04 dated July 16, 2004 effectively modifies and supersedes the 2001 Rulings by stating that the [1997] Tax Code is clear that the "term public means borrowing from twenty (20) or more individual or corporate lenders at any one time." The word "any"

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48 Id. at 1069.
49 Id. at 28.
50 Id.
51 Id.
52 Id. at 577–583.
53 Id. at 611–613.
54 Id. at 614–619.

> plainly indicates that the period contemplated is the entire term of the bond, and not merely the point of origination or issuance. . . . Thus, by taking the PEACe bonds out of the ambit of deposits [sic] substitutes and exempting it from the 20% Final Tax, an exemption in favour of the PEACe Bonds was created when no such exemption is found in the law.[55]

On October 11, 2011, a "Memo for Trading Participants No. 58-2011 was issued by the Philippine Dealing System Holdings Corporation and Subsidiaries ("PDS Group"). The Memo provides that in view of the pronouncement of the DOF and the BIR on the applicability of the 20% FWT on the Government Bonds, no transfer of the same shall be allowed to be recorded in the Registry of Scripless Securities ("ROSS") from 12 October 2011 until the redemption payment date on 18 October 2011. Thus, the bondholders of record appearing on the ROSS as of 18 October 2011, which include the Petitioners, shall be treated by the BTr as the beneficial owners of such securities for the relevant [tax] payments to be imposed thereon."[56]

On October 17, 2011, replying to an urgent query from the Bureau of Treasury, the Bureau of Internal Revenue issued **BIR Ruling No. DA 378-2011**[57] clarifying that the final withholding tax due on the discount or interest earned on the PEACe Bonds should "be imposed and withheld not only on RCBC/CODE NGO but also [on] 'all subsequent holders of the Bonds.'"[58]

On October 17, 2011, petitioners filed a petition for certiorari, prohibition, and/or mandamus (with urgent application for a temporary restraining order and/or writ of preliminary injunction)[59] before this court.

On October 18, 2011, this court issued a temporary restraining order (TRO)[60] "enjoining the implementation of BIR Ruling No. 370-2011 against the [PEACe Bonds,] . . . subject to the condition that the 20% final withholding tax on interest income therefrom shall be withheld by the petitioner banks and placed in escrow pending resolution of [the] petition."[61]

On October 28, 2011, RCBC and RCBC Capital filed a motion for leave of court to intervene and to admit petition-in-intervention[62] dated October 27, 2011, which was granted by this court on November 15, 2011.[63]

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55 Id. at 124–125.
56 Id. at 29–30.
57 Id. at 634–637.
58 Id. at 637.
59 Id. at 13–83.
60 Id. at 235–237.
61 Id. at 236.
62 Id. at 950–1042.
63 Id. at 1164–1166.

Meanwhile, on November 9, 2011, petitioners filed their "Manifestation with Urgent Ex Parte Motion to Direct Respondents to Comply with the TRO."[64] They alleged that on the same day that the temporary restraining order was issued, the Bureau of Treasury paid to petitioners and other bondholders the amounts representing the face value of the Bonds, net however of the amounts corresponding to the 20% final withholding tax on interest income, and that the Bureau of Treasury refused to release the amounts corresponding to the 20% final withholding tax.[65]

On November 15, 2011, this court directed respondents to: "(1) SHOW CAUSE why they failed to comply with the October 18, 2011 resolution; and (2) COMPLY with the Court's resolution in order that petitioners may place the corresponding funds in escrow pending resolution of the petition."[66]

On the same day, CODE-NGO filed a motion for leave to intervene (and to admit attached petition-in-intervention with comment on the petition-in-intervention of RCBC and RCBC Capital).[67] The motion was granted by this court on November 22, 2011.[68]

On December 1, 2011, public respondents filed their compliance.[69] They explained that: 1) "the implementation of [BIR Ruling No. 370-2011], which has already been performed on October 18, 2011 with the withholding of the 20% final withholding tax on the face value of the PEACe bonds, is already *fait accompli* . . . when the Resolution and TRO were served to and received by respondents BTr and National Treasurer [on October 19, 2011]";[70] and 2) the withheld amount has *ipso facto* become public funds and cannot be disbursed or released to petitioners without congressional appropriation.[71] Respondents further aver that "[i]nasmuch as the . . . TRO has already become moot . . . the condition attached to it, i.e., 'that the 20% final withholding tax on interest income therefrom shall be withheld by the banks and placed in escrow . . .' has also been rendered moot[.]"[72]

On December 6, 2011, this court noted respondents' compliance.[73]

On February 22, 2012, respondents filed their consolidated comment[74] on the petitions-in-intervention filed by RCBC and RCBC Capital and

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64 Id. at 1094–1109.
65 Id. at 1097–1098.
66 Id. at 1164.
67 Id. at 1176–1240.
68 Id. at 1306–1307.
69 Id. at 1315–1333.
70 Id. at 1319.
71 Id. at 1327–1328.
72 Id. at 1330.
73 Id. at 1346–1347.
74 Id. at 1712–1767.

CODE-NGO.

On November 27, 2012, petitioners filed their "Manifestation with Urgent Reiterative Motion (To Direct Respondents to Comply with the Temporary Restraining Order)."[75]

On December 4, 2012, this court: (a) noted petitioners' manifestation with urgent reiterative motion (to direct respondents to comply with the temporary restraining order); and (b) required respondents to comment thereon.[76]

Respondents' comment[77] was filed on April 15, 2013, and petitioners filed their reply[78] on June 5, 2013.

Issues

The main issues to be resolved are:

I. Whether the PEACe Bonds are "deposit substitutes" and thus subject to 20% final withholding tax under the 1997 National Internal Revenue Code. Related to this question is the interpretation of the phrase "borrowing from twenty (20) or more individual or corporate lenders at any one time" under Section 22(Y) of the 1997 National Internal Revenue Code, particularly on whether the reckoning of the 20 lenders includes trading of the bonds in the secondary market; and

II. If the PEACe Bonds are considered "deposit substitutes," whether the government or the Bureau of Internal Revenue is estopped from imposing and/or collecting the 20% final withholding tax from the face value of these Bonds

   a. Will the imposition of the 20% final withholding tax violate the non-impairment clause of the Constitution?

   b. Will it constitute a deprivation of property without due process of law?

   c. Will it violate Section 245 of the 1997 National Internal Revenue Code on non-retroactivity of rulings?

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75 Id. at 1938–1962.
76 Id. at 1965.
77 Id. at 1995–2007.
78 Id. at 2044–2058.

Arguments of petitioners, RCBC and RCBC Capital, and CODE-NGO

Petitioners argue that "[a]s the issuer of the Government Bonds acting through the BTr, the Government is obligated . . . to pay the face value amount of PhP35 Billion upon maturity without any deduction whatsoever."[79] They add that "the Government cannot impair the efficacy of the [Bonds] by arbitrarily, oppressively and unreasonably imposing the withholding of 20% FWT upon the [Bonds] a mere eleven (11) days before maturity and after several, consistent categorical declarations that such bonds are exempt from the 20% FWT, without violating due process"[80] and the constitutional principle on non-impairment of contracts.[81] Petitioners aver that at the time they purchased the Bonds, they had the right to expect that they would receive the full face value of the Bonds upon maturity, in view of the 2001 BIR Rulings.[82] "[R]egardless of whether or not the 2001 BIR Rulings are correct, the fact remains that [they] relied [on] good faith thereon."[83]

At any rate, petitioners insist that the PEACe Bonds are not deposit substitutes as defined under Section 22(Y) of the 1997 National Internal Revenue Code because there was only one lender (RCBC) to whom the Bureau of Treasury issued the Bonds.[84] They allege that the 2004, 2005, and 2011 BIR Rulings "erroneously interpreted that the number of investors that participate in the 'secondary market' is the determining factor in reckoning the existence or non-existence of twenty (20) or more individual or corporate lenders."[85] Furthermore, they contend that the Bureau of Internal Revenue unduly expanded the definition of deposit substitutes under Section 22 of the 1997 National Internal Revenue Code in concluding that "the mere issuance of government debt instruments and securities is deemed as falling within the coverage of 'deposit substitutes[.]'"[86] Thus, "[t]he 2011 BIR Ruling clearly amount[ed] to an unauthorized act of administrative legislation[.]"[87]

Petitioners further argue that their income from the Bonds is a "trading gain," which is exempt from income tax.[88] They insist that "[t]hey are not lenders whose income is considered as 'interest income or yield' subject to the 20% FWT under Section 27 (D)(1) of the [1997 National Internal Revenue Code]"[89] because they "acquired the Government Bonds in

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79 Id. at 50.
80 Id.
81 Id.
82 Id. at 45.
83 Id.
84 Id. at 46–47.
85 Id. at 47.
86 Id. at 53.
87 Id. at 54.
88 Id. at 43.
89 Id.

the secondary or tertiary market."[90]

Even assuming without admitting that the Government Bonds are deposit substitutes, petitioners argue that the collection of the final tax was barred by prescription.[91] They point out that under Section 7 of DOF Department Order No. 141-95,[92] the final withholding tax "should have been withheld at the time of their issuance[.]"[93] Also, under Section 203 of the 1997 National Internal Revenue Code, "internal revenue taxes, such as the final tax, [should] be assessed within three (3) years after the last day prescribed by law for the filing of the return."[94]

Moreover, petitioners contend that the retroactive application of the 2011 BIR Ruling without prior notice to them was in violation of their property rights,[95] their constitutional right to due process[96] as well as Section 246 of the 1997 National Internal Revenue Code on non-retroactivity of rulings.[97] Allegedly, it would also have "an adverse effect of colossal magnitude on the investors, both local and foreign, the Philippine capital market, and most importantly, the country's standing in the international commercial community."[98] Petitioners explained that "unless enjoined, the government's threatened refusal to pay the full value of the Government Bonds will negatively impact on the image of the country in terms of protection for property rights (including financial assets), degree of legal protection for lender's rights, and strength of investor protection."[99] They cited the country's ranking in the World Economic Forum: 75th in the world in its 2011–2012 Global Competitiveness Index, 111th out of 142 countries worldwide and 2nd to the last among ASEAN countries in terms of Strength of Investor Protection, and 105th worldwide and last among ASEAN countries in terms of Property Rights Index and Legal Rights Index.[100] It would also allegedly "send a reverberating message to the whole world that there is no certainty, predictability, and stability of financial transactions in the capital markets[.]"[101] "[T]he integrity of Government-issued bonds and notes will be greatly shattered and the credit of the Philippine Government will suffer"[102] if the sudden turnaround of the government will be allowed,[103] and it will reinforce "investors' perception that the level of regulatory risk for contracts entered into by the Philippine Government is high,"[104] thus

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90 Id.
91 Id. at 49.
92 Revised Rules and Regulations for the Issuance, Placement, Sale, Service and Redemption of the Treasury Bills and Bonds Under R.A. No. 245, as amended (2004).
93 Id. at 48.
94 Id. at 49.
95 Id. at 54.
96 Id. at 58.
97 Id. at 54–55.
98 Id. at 55.
99 Id. at 63.
100 Id. at 64–65 and 185–210.
101 Id. at 66.
102 Id. at 67.
103 Id.
104 Id. at 69.

resulting in higher interest rate for government-issued debt instruments and lowered credit rating.[105]

Petitioners-intervenors RCBC and RCBC Capital contend that respondent Commissioner of Internal Revenue "gravely and seriously abused her discretion in the exercise of her rule-making power"[106] when she issued the assailed 2011 BIR Ruling which ruled that "all treasury bonds are 'deposit substitutes' regardless of the number of lenders, in clear disregard of the requirement of twenty (20) or more lenders mandated under the NIRC."[107] They argue that "[b]y her blanket and arbitrary classification of treasury bonds as deposit substitutes, respondent CIR not only amended and expanded the NIRC, but effectively imposed a new tax on privately-placed treasury bonds."[108] Petitioners-intervenors RCBC and RCBC Capital further argue that the 2011 BIR Ruling will cause substantial impairment of their vested rights[109] under the Bonds since the ruling imposes new conditions by "subjecting the PEACe Bonds to the twenty percent (20%) final withholding tax notwithstanding the fact that the terms and conditions thereof as previously represented by the Government, through respondents BTr and BIR, expressly state that it is not subject to final withholding tax upon their maturity."[110] They added that "[t]he exemption from the twenty percent (20%) final withholding tax [was] the primary inducement and principal consideration for [their] participat[ion] in the auction and underwriting of the PEACe Bonds."[111]

Like petitioners, petitioners-intervenors RCBC and RCBC Capital also contend that respondent Commissioner of Internal Revenue violated their rights to due process when she arbitrarily issued the 2011 BIR Ruling without prior notice and hearing, and the oppressive timing of such ruling deprived them of the opportunity to challenge the same.[112]

Assuming the 20% final withholding tax was due on the PEACe Bonds, petitioners-intervenors RCBC and RCBC Capital claim that respondents Bureau of Treasury and CODE-NGO should be held liable "as [these] parties explicitly represented . . . that the said bonds are exempt from the final withholding tax."[113]

Finally, petitioners-intervenors RCBC and RCBC Capital argue that "the implementation of the [2011 assailed BIR Ruling and BIR Ruling No. DA 378-2011] will have pernicious effects on the integrity of existing

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105 Id.
106 Id. at 1004.
107 Id.
108 Id. at 1005.
109 Id. at 1020.
110 Id. at 1013.
111 Id. at 1014.
112 Id. at 1015–1019.
113 Id. at 1032–1033.

securities, which is contrary to the State policies of stabilizing the financial system and of developing capital markets."[114]

For its part, CODE-NGO argues that: (a) the 2011 BIR Ruling and BIR Ruling No. DA 378-2011 are "invalid because they contravene Section 22(Y) of the 1997 [NIRC] when the said rulings disregarded the applicability of the '20 or more lender' rule to government debt instruments"[;][115] (b) "when [it] sold the PEACe Bonds in the secondary market instead of holding them until maturity, [it] derived . . . long-term trading gain[s], not interest income, which [are] exempt . . . under Section 32(B)(7)(g) of the 1997 NIRC"[;][116] (c) "the tax exemption privilege relating to the issuance of the PEACe Bonds . . . partakes of a contractual commitment granted by the Government in exchange for a valid and material consideration [i.e., the issue price paid and savings in borrowing cost derived by the Government,] thus protected by the non-impairment clause of the 1987 Constitution"[;][117] and (d) the 2004, 2005, and 2011 BIR Rulings "did not validly revoke the 2001 BIR Rulings since no notice of revocation was issued to [it], RCBC and [RCBC Capital] and petitioners[-bondholders], nor was there any BIR administrative guidance issued and published[.]"[118] CODE-NGO additionally argues that impleading it in a Rule 65 petition was improper because: (a) it involves determination of a factual question;[119] and (b) it is premature and states no cause of action as it amounts to an anticipatory third-party claim.[120]

Arguments of respondents

Respondents argue that petitioners' direct resort to this court to challenge the 2011 BIR Ruling violates the doctrines of exhaustion of administrative remedies and hierarchy of courts, resulting in a lack of cause of action that justifies the dismissal of the petition.[121] According to them, "the jurisdiction to review the rulings of the [Commissioner of Internal Revenue], after the aggrieved party exhausted the administrative remedies, pertains to the Court of Tax Appeals."[122] They point out that "a case similar to the present Petition was [in fact] filed with the CTA on October 13, 2011[,] [docketed as] CTA Case No. 8351 [and] entitled, 'Rizal Commercial Banking Corporation and RCBC Capital Corporation vs. Commissioner of Internal Revenue, et al.'"[123]

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114 Id. at 1033.
115 Id. at 1212.
116 Id. at 1215.
117 Id. at 1218.
118 Id. at 1222.
119 Id. at 1235.
120 Id. at 1235–1236.
121 Id. at 315–331.
122 Id. at 328.
123 Id. at 331. The case docketed as CTA Case No. 8351 was deemed withdrawn based on the ruling of the Court of Tax Appeals in the resolution dated October 28, 2011 and which became final and executory on December 8, 2011. The RCBC and RCBC Capital filed the notice of withdrawal of the petition.

Respondents further take issue on the timeliness of the filing of the petition and petitions-in-intervention.[124] They argue that under the guise of mainly assailing the 2011 BIR Ruling, petitioners are indirectly attacking the 2004 and 2005 BIR Rulings, of which the attack is legally prohibited, and the petition insofar as it seeks to nullify the 2004 and 2005 BIR Rulings was filed way out of time pursuant to Rule 65, Section 4.[125]

Respondents contend that the discount/interest income derived from the PEACe Bonds is not a trading gain but interest income subject to income tax.[126] They explain that "[w]ith the payment of the PhP35 Billion proceeds on maturity of the PEACe Bonds, Petitioners receive an amount of money equivalent to about PhP24.8 Billion as payment for interest. Such interest is clearly an income of the Petitioners considering that the same is a flow of wealth and not merely a return of capital – the capital initially invested in the Bonds being approximately PhP10.2 Billion[.]"[127]

Maintaining that the imposition of the 20% final withholding tax on the PEACe Bonds does not constitute an impairment of the obligations of contract, respondents aver that: "The BTr has no power to contractually grant a tax exemption in favour of Petitioners thus the 2001 BIR Rulings cannot be considered a material term of the Bonds"[;][128] "[t]here has been no change in the laws governing the taxability of interest income from deposit substitutes and said laws are read into every contract"[;][129] "[t]he assailed BIR Rulings merely interpret the term "deposit substitute" in accordance with the letter and spirit of the Tax Code"[;][130] "[t]he withholding of the 20% FWT does not result in a default by the Government as the latter performed its obligations to the bondholders in full"[;][131] and "[i]f there was a breach of contract or a misrepresentation it was between RCBC/CODE-NGO/RCBC Cap and the succeeding purchasers of the PEACe Bonds."[132]

Similarly, respondents counter that the withholding of "[t]he 20% final withholding tax on the PEACe Bonds does not amount to a deprivation of property without due process of law."[133] Their imposition of the 20% final withholding tax is not arbitrary because they were only performing a duty imposed by law;[134] "[t]he 2011 BIR Ruling is an interpretative rule which merely interprets the meaning of deposit substitutes [and upheld] the earlier

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124 Id. at 331–333 and 1716.
125 Id. at 332–333.
126 Id. at 333–336.
127 Id. at 339.
128 Id. at 342.
129 Id. at 344.
130 Id. at 346.
131 Id. at 350.
132 Id. at 351.
133 Id. at 354.
134 Id. at 357.

construction given to the term by the 2004 and 2005 BIR Rulings."[135] Hence, respondents argue that "there was no need to observe the requirements of notice, hearing, and publication[.]"[136]

Nonetheless, respondents add that "there is every reason to believe that Petitioners — all major financial institutions equipped with both internal and external accounting and compliance departments as well as access to both internal and external legal counsel; actively involved in industry organizations such as the Bankers Association of the Philippines and the Capital Market Development Council; all actively taking part in the regular and special debt issuances of the BTr and indeed regularly proposing products for issue by BTr — had actual notice of the 2004 and 2005 BIR Rulings."[137] Allegedly, "the sudden and drastic drop — including virtually zero trading for extended periods of six months to almost a year — in the trading volume of the PEACe Bonds after the release of BIR Ruling No. 007-04 on July 16, 2004 tend to indicate that market participants, including the Petitioners herein, were aware of the ruling and its consequences for the PEACe Bonds."[138]

Moreover, they contend that the assailed 2011 BIR Ruling is a valid exercise of the Commissioner of Internal Revenue's rule-making power;[139] that it and the 2004 and 2005 BIR Rulings did not unduly expand the definition of deposit substitutes by creating an unwarranted exception to the requirement of having 20 or more lenders/purchasers;[140] and the word "any" in Section 22(Y) of the National Internal Revenue Code plainly indicates that the period contemplated is the entire term of the bond and not merely the point of origination or issuance.[141]

Respondents further argue that a retroactive application of the 2011 BIR Ruling will not unjustifiably prejudice petitioners.[142] "[W]ith or without the 2011 BIR Ruling, Petitioners would be liable to pay a 20% final withholding tax just the same because the PEACe Bonds in their possession are legally in the nature of deposit substitutes subject to a 20% final withholding tax under the NIRC."[143] Section 7 of DOF Department Order No. 141-95 also provides that income derived from Treasury bonds is subject to the 20% final withholding tax.[144] "[W]hile revenue regulations as a general rule have no retroactive effect, if the revocation is due to the fact that the regulation is erroneous or contrary to law, such revocation shall have

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135 Id. at 362.
136 Id. at 370.
137 Id.
138 Id.
139 Id. at 360.
140 Id. at 362.
141 Id. at 366.
142 Id. at 383.
143 Id. at 384.
144 Id. at 392.

retroactive operation as to affect past transactions, because a wrong construction of the law cannot give rise to a vested right that can be invoked by a taxpayer."[145]

Finally, respondents submit that "there are a number of variables and factors affecting a capital market."[146] "[C]apital market itself is inherently unstable."[147] Thus, "[p]etitioners' argument that the 20% final withholding tax . . . will wreak havoc on the financial stability of the country is a mere supposition that is not a justiciable issue."[148]

On the prayer for the temporary restraining order, respondents argue that this order "could no longer be implemented [because] the acts sought to be enjoined are already *fait accompli*."[149] They add that "to disburse the funds withheld to the Petitioners at this time would violate Section 29[,] Article VI of the Constitution prohibiting 'money being paid out of the Treasury except in pursuance of an appropriation made by law[.]'"[150] "The remedy of petitioners is to claim a tax refund under Section 204(c) of the Tax Code should their position be upheld by the Honorable Court."[151]

Respondents also argue that "the implementation of the TRO would violate Section 218 of the Tax Code in relation to Section 11 of Republic Act No. 1125 (as amended by Section 9 of Republic Act No. 9282) which prohibits courts, except the Court of Tax Appeals, from issuing injunctions to restrain the collection of any national internal revenue tax imposed by the Tax Code."[152]

Summary of arguments

In sum, petitioners and petitioners-intervenors, namely, RCBC, RCBC Capital, and CODE-NGO argue that:

1. The 2011 BIR Ruling is ultra vires because it is contrary to the 1997 National Internal Revenue Code when it declared that all government debt instruments are deposit substitutes regardless of the 20-lender rule; and

2. The 2011 BIR Ruling cannot be applied retroactively because:

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145 Id. at 384–385.
146 Id. at 393.
147 Id.
148 Id. at 392.
149 Id. at 394.
150 Id. at 396.
151 Id. at 396–397.
152 Id. at 397.

a) It will violate the contract clause;

- It constitutes a unilateral amendment of a material term (tax exempt status) in the Bonds, represented by the government as an inducement and important consideration for the purchase of the Bonds;

b) It constitutes deprivation of property without due process because there was no prior notice to bondholders and hearing and publication;

c) It violates the rule on non-retroactivity under the 1997 National Internal Revenue Code;

d) It violates the constitutional provision on supporting activities of non-government organizations and development of the capital market; and

e) The assessment had already prescribed.

Respondents counter that:

1) Respondent Commissioner of Internal Revenue did not act with grave abuse of discretion in issuing the challenged 2011 BIR Ruling:

a. The 2011 BIR Ruling, being an interpretative rule, was issued by virtue of the Commissioner of Internal Revenue's power to interpret the provisions of the 1997 National Internal Revenue Code and other tax laws;

b. Commissioner of Internal Revenue merely restates and confirms the interpretations contained in previously issued BIR Ruling Nos. 007-2004, DA-491-04, and 008-05, which have already effectively abandoned or revoked the 2001 BIR Rulings;

c. Commissioner of Internal Revenue is not bound by his or her predecessor's rulings especially when the latter's rulings are not in harmony with the law; and

d. The wrong construction of the law that the 2001 BIR Rulings have perpetrated cannot give rise to a vested right. Therefore, the 2011 BIR Ruling can be given retroactive effect.

2) Rule 65 can be resorted to only if there is no appeal or any plain, speedy, and adequate remedy in the ordinary course of law:

a. Petitioners had the basic remedy of filing a claim for refund of the 20% final withholding tax they allege to have been wrongfully collected; and

b. Non-observance of the doctrine of exhaustion of administrative remedies and of hierarchy of courts.

Court's ruling

Procedural Issues

Non-exhaustion of administrative remedies proper

Under Section 4 of the 1997 National Internal Revenue Code, interpretative rulings are reviewable by the Secretary of Finance.

> **SEC. 4. Power of the Commissioner to Interpret Tax Laws and to Decide Tax Cases. -** *The power to interpret the provisions of this Code and other tax laws shall be under the exclusive and original jurisdiction of the Commissioner, subject to review by the Secretary of Finance.* (Emphasis supplied)

Thus, it was held that "[i]f superior administrative officers [can] grant the relief prayed for, [then] special civil actions are generally not entertained."[153] The remedy within the administrative machinery must be resorted to first and pursued to its appropriate conclusion before the court's judicial power can be sought.[154]

Nonetheless, jurisprudence allows certain exceptions to the rule on exhaustion of administrative remedies:

> [The doctrine of exhaustion of administrative remedies] is a relative one and its flexibility is called upon by the peculiarity and uniqueness of the factual and circumstantial settings of a case. Hence, it is disregarded (1) when there is a violation of due process, (2) *when the issue involved is purely a legal question*,[155] (3) when the administrative action is

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153 *Militante v. Court of Appeals,* 386 Phil. 522, 538 (2000) [Per J. Puno, En Banc], *cited in Gorospe v. Vinzons-Chato*, G.R. No. 132228, January 21, 2003 <http://nlpdl.nlp.gov.ph:9000/rpc/cat/finders/SC02/2003jan/132228.htm> [En Banc].

154 *Asia International Auctioneers, Inc. v. Hon. Parayno, Jr.,* 565 Phil. 255, 270 (2007) [Per C.J. Puno, First Division]; *Laguna CATV Network, Inc. v. Hon. Maraan*, 440 Phil. 734, 741 (2002) [Per J. Sandoval-Gutierrez, Third Division].

155 *Dueñas v. Santos Subdivision Homeowners Association*, G.R. No. 149417, June 4, 2004, 431 SCRA 76, 84–85 [Per J. Quisumbing,Second Division]; *Republic of the Philippines v. Lacap,* 546 Phil. 87, 97

> patently illegal amounting to lack or excess of jurisdiction,(4) when there is estoppel on the part of the administrative agency concerned,(5) when there is irreparable injury, (6) when the respondent is a department secretary whose acts as an alter ego of the President bears the implied and assumed approval of the latter, (7) when to require exhaustion of administrative remedies would be unreasonable, (8) when it would amount to a nullification of a claim, (9) when the subject matter is a private land in land case proceedings, (10) when the rule does not provide a plain, speedy and adequate remedy, (11) *when there are circumstances indicating the urgency of judicial intervention*.[156] (Emphasis supplied, citations omitted)

The exceptions under (2) and (11) are present in this case. The question involved is purely legal, namely: (a) the interpretation of the 20-lender rule in the definition of the terms *public* and *deposit substitutes* under the 1997 National Internal Revenue Code; and (b) whether the imposition of the 20% final withholding tax on the PEACe Bonds upon maturity violates the constitutional provisions on non-impairment of contracts and due process. Judicial intervention is likewise urgent with the impending maturity of the PEACe Bonds on October 18, 2011.

The rule on exhaustion of administrative remedies also finds no application when the exhaustion will result in an exercise in futility.[157]

In this case, an appeal to the Secretary of Finance from the questioned 2011 BIR Ruling would be a futile exercise because it was upon the request of the Secretary of Finance that the 2011 BIR Ruling was issued by the Bureau of Internal Revenue. It appears that the Secretary of Finance adopted the Commissioner of Internal Revenue's opinions as his own.[158] This position was in fact confirmed in the letter[159] dated October 10, 2011 where he ordered the Bureau of Treasury to withhold the amount corresponding to the 20% final withholding tax on the interest or discounts allegedly due from the bondholders on the strength of the 2011 BIR Ruling.

Doctrine on hierarchy of courts

We agree with respondents that the jurisdiction to review the rulings of the Commissioner of Internal Revenue pertains to the Court of Tax Appeals. The questioned BIR Ruling Nos. 370-2011 and DA 378-2011 were issued in connection with the implementation of the 1997 National Internal

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(2007) [Per J. Austria-Martinez, Third Division]; *Cebu Oxygen and Acetylene Co., Inc. (COACO) v. Secretary Drilon*, 257 Phil. 23, 29 (1989) [Per J. Gancayco, En Banc].

156 *Paat v. Court of Appeals*, 334 Phil. 146, 153 (1997) [Per J. Torres, Jr., Second Division].

157 *Castro v. Sec. Gloria*, 415 Phil. 645, 652 (2001) [Per J. Sandoval-Gutierrez, Third Division].

158 DOF News Correspondent, *PEACe Bonds Subject to 20% Final Withholding Tax*, October 7, 2011 <http://www.dof.gov.ph/?p=3199> (visited January 27, 2015): "Sought for comment, Finance Secretary Cesar V. Purisima stated that the recent BIR Ruling merely confirms that existing rulings on the tax treatment of Treasury Bills and Treasury Bonds apply to the PEACe Bonds and provides appropriate legal basis for the Treasury to withhold the tax."

159 *Rollo*, p. 1114.

Revenue Code on the taxability of the interest income from zero-coupon bonds issued by the government.

Under Republic Act No. 1125 (An Act Creating the Court of Tax Appeals), as amended by Republic Act No. 9282,[160] such rulings of the Commissioner of Internal Revenue are appealable to that court, thus:

> SEC. 7. *Jurisdiction.* - The CTA shall exercise:
>
> a. *Exclusive appellate jurisdiction to review by appeal*, as herein provided:
>
> 1. *Decisions of the Commissioner of Internal Revenue in* cases involving disputed assessments, refunds of internal revenue taxes, fees or other charges, penalties in relation thereto, or other *matters arising under the National Internal Revenue or other laws administered by the Bureau of Internal Revenue*;
>
> . . . .
>
> SEC. 11. *Who May Appeal; Mode of Appeal; Effect of Appeal. - Any party adversely affected by a decision, ruling or inaction of the Commissioner of Internal Revenue*, the Commissioner of Customs, the Secretary of Finance, the Secretary of Trade and Industry or the Secretary of Agriculture or the Central Board of Assessment Appeals or the Regional Trial Courts *may file an appeal with the CTA within thirty (30) days after the receipt of such decision or ruling* or after the expiration of the period fixed by law for action as referred to in Section 7(a)(2) herein.
>
> . . . .
>
> SEC. 18. *Appeal to the Court of Tax Appeals En Banc. - No civil proceeding involving matters arising under the National Internal Revenue Code*, the Tariff and Customs Code or the Local Government Code *shall be maintained, except as herein provided, until and unless an appeal has been previously filed with the CTA and disposed of in accordance with the provisions of this Act.*

In *Commissioner of Internal Revenue v. Leal*,[161] citing *Rodriguez v. Blaquera,*[162] this court emphasized the jurisdiction of the Court of Tax Appeals over rulings of the Bureau of Internal Revenue, thus:

> While the Court of Appeals correctly took cognizance of the

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160 An Act Expanding the Jurisdiction of the Court of Tax Appeals (CTA), Elevating its Rank to the Level of a Collegiate Court with Special Jurisdiction and Enlarging its Membership, Amending for the Purpose Certain Sections of Republic Act No. 1125, As Amended, Otherwise Known as The Law Creating the Court of Tax Appeals, and for Other Purposes (2004).

161 440 Phil. 477 (2002) [Per Sandoval-Gutierrez, Third Division], *cited in Asia International Auctioneers, Inc. v. Hon. Parayno, Jr.*, 565 Phil. 255, 268–269 (2007) [Per C.J. Puno, First Division].

162 109 Phil. 598 (1960) [Per J. Concepcion, En Banc].

petition for *certiorari*, however, *let it be stressed that the jurisdiction to review the rulings of the Commissioner of Internal Revenue pertains to the Court of Tax Appeals, not to the RTC.*

The questioned RMO No. 15-91 and RMC No. 43-91 are actually rulings or opinions of the Commissioner implementing the Tax Code on the taxability of pawnshops. . . .

. . . .

Such revenue orders were issued pursuant to petitioner's powers under Section 245 of the Tax Code, which states:

> "SEC. 245. *Authority of the Secretary of Finance to promulgate rules and regulations.* — The Secretary of Finance, upon recommendation of the Commissioner, shall promulgate all needful rules and regulations for the effective enforcement of the provisions of this Code.
>
> The authority of the Secretary of Finance to determine articles similar or analogous to those subject to a rate of sales tax under certain category enumerated in Section 163 and 165 of this Code shall be without prejudice to *the power of the Commissioner of Internal Revenue to make rulings or opinions in connection with the implementation of the provisions of internal revenue laws, including ruling on the classification of articles of sales and similar purposes.*" (Emphasis in the original)

. . . .

The Court, in *Rodriguez, etc. vs. Blaquera, etc*., ruled:

> "Plaintiff maintains that this is not an appeal from a ruling of the Collector of Internal Revenue, but merely an attempt to nullify General Circular No. V-148, which does not adjudicate or settle any controversy, and that, accordingly, this case is not within the jurisdiction of the Court of Tax Appeals.
>
> We find no merit in this pretense. General Circular No. V-148 directs the officers charged with the collection of taxes and license fees to adhere strictly to the interpretation given by the defendant to the statutory provisions abovementioned, as set forth in the Circular. The same incorporates, therefore, a decision of the Collector of Internal Revenue (now Commissioner of Internal Revenue) on the manner of enforcement of the said statute, the administration of which is entrusted by law to the Bureau of Internal Revenue. As such, it comes within the purview of Republic Act No. 1125, Section 7 of which provides that the Court of Tax Appeals 'shall exercise exclusive appellate jurisdiction to review by appeal . . . decisions of the Collector of Internal Revenue in . . . matters arising under the National Internal Revenue Code or other law or part of the law administered by the Bureau of Internal

Revenue.'"[163]

In exceptional cases, however, this court entertained direct recourse to it when "dictated by public welfare and the advancement of public policy, or demanded by the broader interest of justice, or the orders complained of were found to be patent nullities, or the appeal was considered as clearly an inappropriate remedy."[164]

In *Philippine Rural Electric Cooperatives Association, Inc. (PHILRECA) v. The Secretary, Department of Interior and Local Government,*[165] this court noted that the petition for prohibition was filed directly before it "in disregard of the rule on hierarchy of courts. However, [this court] opt[ed] to take primary jurisdiction over the . . . petition and decide the same on its merits in view of the significant constitutional issues raised by the parties dealing with the tax treatment of cooperatives under existing laws and in the interest of speedy justice and prompt disposition of the matter."[166]

Here, the nature and importance of the issues raised[167] to the investment and banking industry with regard to a definitive declaration of whether government debt instruments are deposit substitutes under existing laws, and the novelty thereof, constitute exceptional and compelling circumstances to justify resort to this court in the first instance.

The tax provision on deposit substitutes affects not only the PEACe Bonds but also any other financial instrument or product that may be issued and traded in the market. Due to the changing positions of the Bureau of Internal Revenue on this issue, there is a need for a final ruling from this court to stabilize the expectations in the financial market.

Finally, non-compliance with the rules on exhaustion of administrative remedies and hierarchy of courts had been rendered moot by this court's issuance of the temporary restraining order enjoining the implementation of the 2011 BIR Ruling. The temporary restraining order effectively recognized the urgency and necessity of direct resort to this court.

Substantive issues

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163 *Commissioner of Internal Revenue v. Leal*, 440 Phil. 477, 485–487 (2002) [Per J. Sandoval-Gutierrez, Third Division].

164 *Congressman Chong, et al. v. Hon. Dela Cruz, et al.*, 610 Phil. 725, 728 (2009) [Per J. Nachura, Third Division].

165 451 Phil. 683 (2003) [Per J. Puno, En Banc].

166 Id. at 689.

167 *See John Hay Peoples Alternative Coalition v. Lim*, 460 Phil. 530, 542–543 (2003) [Per J. Carpio Morales, En Banc].

Tax treatment of deposit substitutes

Under Sections 24(B)(1), 27(D)(1), and 28(A)(7) of the 1997 National Internal Revenue Code, a final withholding tax at the rate of 20% is imposed on interest on any currency bank deposit and yield or any other monetary benefit from deposit substitutes and from trust funds and similar arrangements. These provisions read:

> **SEC. 24. Income Tax Rates**.
>
> . . . .
>
> (B) Rate of Tax on Certain Passive Income.
>
> (1) Interests, Royalties, Prizes, and Other Winnings. - *A final tax at the rate of twenty percent (20%) is hereby imposed upon the amount of interest from any currency bank deposit and yield or any other monetary benefit from deposit substitutes* and from trust funds and similar arrangements; . . . Provided, further, That interest income from long-term deposit or investment in the form of savings, common or individual trust funds, deposit substitutes, investment management accounts and other investments evidenced by certificates in such form prescribed by the Bangko Sentral ng Pilipinas (BSP) shall be exempt from the tax imposed under this Subsection: Provided, finally, That should the holder of the certificate pre-terminate the deposit or investment before the fifth (5th) year, a final tax shall be imposed on the entire income and shall be deducted and withheld by the depository bank from the proceeds of the long-term deposit or investment certificate based on the remaining maturity thereof:
>
> Four (4) years to less than five (5) years - 5%;
> Three (3) years to less than four (4) years - 12%; and
> Less than three (3) years - 20%. (Emphasis supplied)
>
> **SEC. 27. Rates of Income Tax on Domestic Corporations. -**
>
> . . . .
>
> (D) Rates of Tax on Certain Passive Incomes. -
>
> (1) Interest from Deposits and Yield or any other Monetary Benefit from Deposit Substitutes and from Trust Funds and Similar Arrangements, and Royalties. - *A final tax at the rate of twenty percent (20%) is hereby imposed upon the amount of interest on currency bank deposit and yield or any other monetary benefit from deposit substitutes* and from trust funds and similar arrangements *received by domestic corporations*, and royalties, derived from sources within the Philippines: Provided, however, That interest income derived by a domestic corporation from a depository bank under the expanded foreign

> currency deposit system shall be subject to a final income tax at the rate of seven and one-half percent (7 1/2%) of such interest income. (Emphasis supplied)
>
> **SEC. 28. Rates of Income Tax on Foreign Corporations. -**
>
> (A) Tax on Resident Foreign Corporations. -
>
> . . . .
>
> (7) Tax on Certain Incomes Received by a Resident Foreign Corporation. -
>
> (a) Interest from Deposits and Yield or any other Monetary Benefit from Deposit Substitutes, Trust Funds and Similar Arrangements and Royalties. - *Interest from any currency bank deposit and yield or any other monetary benefit from deposit substitutes and from trust funds and similar arrangements and royalties derived from sources within the Philippines shall be subject to a final income tax at the rate of twenty percent (20%) of such interest*: Provided, however, That interest income derived by a resident foreign corporation from a depository bank under the expanded foreign currency deposit system shall be subject to a final income tax at the rate of seven and one-half percent (7 1/2%) of such interest income. (Emphasis supplied)

This tax treatment of interest from bank deposits and yield from deposit substitutes was first introduced in the 1977 National Internal Revenue Code through Presidential Decree No. 1739[168] issued in 1980. Later, Presidential Decree No. 1959, effective on October 15, 1984, formally added the definition of deposit substitutes, *viz*:

> (y) *'Deposit substitutes'* shall mean *an alternative form of obtaining funds from the public, other than deposits, through the issuance, endorsement, or acceptance of debt instruments* ***for the borrower's own account,*** *for the purpose of relending or purchasing of receivables and other obligations, or financing their own needs or the needs of their agent or dealer***.** These promissory notes, repurchase agreements, certificates of assignment or participation and similar instrument with recourse as may be authorized by the Central Bank of the Philippines, for banks and non-bank financial intermediaries or by the Securities and Exchange Commission of the Philippines for commercial, industrial, finance companies and either non-financial companies: *Provided, however,* that only debt instruments issued for inter-bank call loans to cover deficiency in reserves against deposit liabilities including those between or among banks and quasi-banks shall not be considered as deposit substitute debt instruments. (Emphasis supplied)

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[168] Providing Fiscal Incentives by Amending Certain Provisions of the National Internal Revenue Code, and for Other Purposes (1980).

Revenue Regulations No. 17-84, issued to implement Presidential Decree No. 1959, adopted verbatim the same definition and specifically identified the following borrowings as "deposit substitutes":

> SECTION 2. Definitions of Terms. . . .
>
> (h) "Deposit substitutes" shall mean –
>
> . . . .
>
> (a) All interbank borrowings by or among banks and non-bank financial institutions authorized to engage in quasi-banking functions evidenced by deposit substitutes instruments, except interbank call loans to cover deficiency in reserves against deposit liabilities as evidenced by interbank loan advice or repayment transfer tickets.
>
> *(b) All borrowings of the national and local government and its instrumentalities including the Central Bank of the Philippines, evidenced by debt instruments denoted as treasury bonds, bills, notes, certificates of indebtedness and similar instruments.*
>
> (c) All borrowings of banks, non-bank financial intermediaries, finance companies, investment companies, trust companies, including the trust department of banks and investment houses, evidenced by deposit substitutes instruments. (Emphasis supplied)

The definition of deposit substitutes was amended under the 1997 National Internal Revenue Code with the addition of the qualifying phrase for *public – borrowing from 20 or more individual or corporate lenders at any one time.* Under Section 22(Y), deposit substitute is defined thus:

> **SEC. 22. Definitions** - When used in this Title:
>
> . . . .
>
> (Y) The term **'deposit substitutes'** shall mean *an alternative form of obtaining funds from the public* (***the term 'public' means borrowing from twenty (20) or more individual or corporate lenders at any one time***) other than deposits, *through the issuance, endorsement, or acceptance of debt instruments* ***for the borrower's own account***, for the purpose of relending or purchasing of receivables and other obligations, or financing their own needs or the needs of their agent or dealer. These instruments may include, but need not be limited to, bankers' acceptances, promissory notes, repurchase agreements, including reverse repurchase agreements entered into by and between the Bangko Sentral ng Pilipinas (BSP) and any authorized agent bank, certificates of assignment or participation and similar instruments with recourse: Provided, however, That debt instruments issued for interbank call loans with

> maturity of not more than five (5) days to cover deficiency in reserves against deposit liabilities, including those between or among banks and quasi-banks, shall not be considered as deposit substitute debt instruments. (Emphasis supplied)

Under the 1997 National Internal Revenue Code, Congress specifically defined "public" to mean "twenty (20) or more individual or corporate lenders at any one time." Hence, the number of lenders is determinative of whether a debt instrument should be considered a deposit substitute and consequently subject to the 20% final withholding tax.

20-lender rule

Petitioners contend that "there [is] only one (1) lender (i.e. RCBC) to whom the BTr issued the Government Bonds."[169] On the other hand, respondents theorize that the word "any" "indicates that the period contemplated is the entire term of the bond and not merely the point of origination or issuance[,]"[170] such that if the debt instruments "were subsequently sold in secondary markets and so on, in such a way that twenty (20) or more buyers eventually own the instruments, then it becomes indubitable that funds would be obtained from the "public" as defined in Section 22(Y) of the NIRC."[171] Indeed, in the context of the financial market, the words "at any one time" create an ambiguity.

Financial markets

Financial markets provide the channel through which funds from the surplus units (households and business firms that have savings or excess funds) flow to the deficit units (mainly business firms and government that need funds to finance their operations or growth). They bring suppliers and users of funds together and provide the means by which the lenders transform their funds into financial assets, and the borrowers receive these funds now considered as their financial liabilities. The transfer of funds is represented by a security, such as stocks and bonds. Fund suppliers earn a return on their investment; the return is necessary to ensure that funds are supplied to the financial markets.[172]

"The financial markets that facilitate the transfer of debt securities are commonly classified by the maturity of the securities[,]"[173] namely: (1) the *money market,* which facilitates the flow of short-term funds (with maturities of one year or less); and (2) the *capital market,* which facilitates the flow of

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169 *Rollo*, p. 47.
170 Id. at 346.
171 Id. at 346–347.
172 Jeff Madura, FINANCIAL INSTITUTIONS AND MARKETS 3–4 (9th ed.).
173 Id. at 4.

long-term funds (with maturities of more than one year).[174]

Whether referring to money market securities or capital market securities, transactions occur either in the *primary market* or in the *secondary market*.[175] "**Primary markets** facilitate the issuance of new securities. **Secondary markets** facilitate the trading of existing securities, which allows for a change in the ownership of the securities."[176] The transactions in primary markets exist between issuers and investors, while secondary market transactions exist among investors.[177]

"Over time, the system of financial markets has evolved from simple to more complex ways of carrying out financial transactions."[178] Still, all systems perform one basic function: *the quick mobilization of money from the lenders/investors to the borrowers.*[179]

Fund transfers are accomplished in three ways: (1) direct finance; (2) semidirect finance; and (3) indirect finance.[180]

With **direct financing**, the "borrower and lender meet each other and exchange funds in return for financial assets"[181] (e.g., purchasing bonds directly from the company issuing them). This method provides certain limitations such as: (a) "both borrower and lender must desire to exchange the same amount of funds at the same time"[;][182] and (b) "both lender and borrower must frequently incur substantial information costs simply to find each other."[183]

In **semidirect financing**, a securities broker or dealer brings surplus and deficit units together, thereby reducing information costs.[184] A **broker**[185] is "an individual or financial institution who provides information concerning possible purchases and sales of securities. Either a buyer or a seller of securities may contact a broker, whose job is simply to bring buyers and sellers together."[186] A **dealer**[187] **"**also serves as a middleman between buyers and sellers, but the dealer actually acquires the seller's securities in

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174 Id.
175 Id.
176 Id.
177 Id.
178 Peter S. Rose, MONEY AND CAPITAL MARKETS 33 (1983).
179 Id.
180 Id.
181 Id. at 34.
182 Id.
183 Id.
184 Id. at 35.
185 SECURITIES CODE, sec. 3.3 defines a "*Broker*" as "a person engaged in the business of buying and selling securities for the account of others."
186 Peter S. Rose, MONEY AND CAPITAL MARKETS 35 (1983).
187 SECURITIES CODE, sec. 3.4 defines a "*Dealer*" as "any person who buys and sells securities for his or her own account in the ordinary course of business."

the hope of selling them at a later time at a more favorable price."[188] Frequently, "a dealer will split up a large issue of primary securities into smaller units affordable by . . . buyers . . . and thereby expand the flow of savings into investment."[189] In semidirect financing, "[t]he ultimate lender still winds up holding the borrower's securities, and therefore the lender must be willing to accept the risk, liquidity, and maturity characteristics of the borrower's [debt security]. There still must be a fundamental coincidence of wants and needs between [lenders and borrowers] for semidirect financial transactions to take place."[190]

"The limitations of both direct and semidirect finance stimulated the development of indirect financial transactions, carried out with the help of financial intermediaries"[191] or financial institutions, like banks, investment banks, finance companies, insurance companies, and mutual funds.[192] Financial intermediaries accept funds from surplus units and channel the funds to deficit units.[193] "Depository institutions [such as banks] accept deposits from surplus units and provide credit to deficit units through loans and purchase of [debt] securities."[194] Nondepository institutions, like mutual funds, issue securities of their own (usually in smaller and affordable denominations) to surplus units and at the same time purchase debt securities of deficit units.[195] "By pooling the resources of [small savers, a financial intermediary] can service the credit needs of large firms simultaneously."[196]

The financial market, therefore, is an agglomeration of financial transactions in securities performed by market participants that works to transfer the funds from the surplus units (or investors/lenders) to those who need them (deficit units or borrowers).

Meaning of "at any one time"

Thus, from the point of view of the financial market, the phrase "at any one time" for purposes of determining the "20 or more lenders" would mean every transaction executed in the primary or secondary market in connection with the purchase or sale of securities.

For example, where the financial assets involved are government securities like bonds, the reckoning of "20 or more lenders/investors" is made at any transaction in connection with the purchase or sale of the

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188 Peter S. Rose, MONEY AND CAPITAL MARKETS 35 (1983).
189 Id.
190 Id.
191 Id. at 36.
192 Id.
193 Id.
194 Jeff Madura, FINANCIAL INSTITUTIONS AND MARKETS 14 (9th ed.).
195 Id. at 15.
196 Peter S. Rose, MONEY AND CAPITAL MARKETS 36–37 (1983).

Government Bonds, such as:

1. Issuance by the Bureau of Treasury of the bonds to GSEDs in the primary market;

2. Sale and distribution by GSEDs to various lenders/investors in the secondary market;

3. Subsequent sale or trading by a bondholder to another lender/investor in the secondary market usually through a broker or dealer; or

4. Sale by a financial intermediary-bondholder of its participation interests in the bonds to individual or corporate lenders in the secondary market.

When, through any of the foregoing transactions, funds are simultaneously obtained from 20 or more lenders/investors, there is deemed to be a public borrowing and the bonds at that point in time are deemed deposit substitutes. Consequently, the seller is required to withhold the 20% final withholding tax on the imputed interest income from the bonds.

For debt instruments that are not deposit substitutes, regular income tax applies

It must be emphasized, however, that debt instruments that do not qualify as deposit substitutes under the 1997 National Internal Revenue Code are subject to the regular income tax.

The phrase "all income derived from whatever source" in Chapter VI, *Computation of Gross Income*, Section 32(A) of the 1997 National Internal Revenue Code discloses a legislative policy to include all income not expressly exempted as within the class of taxable income under our laws.

"The definition of gross income is broad enough to include all passive incomes subject to specific tax rates or final taxes."[197] Hence, interest income from deposit substitutes are necessarily part of taxable income. "However, since these passive incomes are already subject to different rates and taxed finally at source, they are no longer included in the computation of gross income, which determines taxable income."[198] "Stated otherwise . . . if there were no withholding tax system in place in this country, this 20 percent

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[197] *Commissioner of Internal Revenue v. Philippine Airlines, Inc.*, 535 Phil. 95, 106 (2006) [Per C.J. Panganiban, First Division].

[198] Id.

portion of the 'passive' income of [creditors/lenders] would actually be paid to the [creditors/lenders] and then remitted by them to the government in payment of their income tax."[199]

This court, in *Chamber of Real Estate and Builders' Associations, Inc. v. Romulo*,[200] explained the rationale behind the withholding tax system:

> The withholding [of tax at source] was devised for three primary reasons: first, to provide the taxpayer a convenient manner to meet his probable income tax liability; second, to ensure the collection of income tax which can otherwise be lost or substantially reduced through failure to file the corresponding returns[;] and third, to improve the government's cash flow. This results in administrative savings, prompt and efficient collection of taxes, prevention of delinquencies and reduction of governmental effort to collect taxes through more complicated means and remedies.[201] (Citations omitted)

"The application of the withholdings system to interest on bank deposits or yield from deposit substitutes is essentially to maximize and expedite the collection of income taxes by requiring its payment at the source."[202]

Hence, when there are 20 or more lenders/investors in a transaction for a specific bond issue, the seller is required to withhold the 20% final income tax on the imputed interest income from the bonds.

Interest income v. gains from sale or redemption

The interest income earned from bonds is not synonymous with the "gains" contemplated under Section 32(B)(7)(g)[203] of the 1997 National Internal Revenue Code, which exempts gains derived from trading, redemption, or retirement of long-term securities from ordinary income tax.

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199 *Commissioner of Internal Revenue v. Solidbank Corp.*, 462 Phil. 96, 107 (2003) [Per J. Panganiban, First Division].

200 *Chamber of Real Estate and Builders' Associations, Inc. v. Romulo*, G.R. No. 160756, March 9, 2010, 614 SCRA 605 [Per J. Corona, En Banc].

201 Id. at 632–633.

202 *Commissioner of Internal Revenue v. Court of Appeals*, G.R. No. 95022, March 23, 1992, 207 SCRA 487, 496 [Per J. Melencio-Herrera, En Banc].

203 Sec. 32. Gross Income. -

. . . .

(B) Exclusions from Gross Income. - The following items shall not be included in gross income and shall be exempt from taxation under this title:

. . . .

(7) Miscellaneous Items. -

. . . .

(g) Gains from the Sale of Bonds, Debentures or other Certificate of Indebtedness. - Gains realized from the sale or exchange or retirement of bonds, debentures or other certificate of indebtedness with a maturity of more than five (5) years.

The term "gain" as used in Section 32(B)(7)(g) does not include interest, which represents forbearance for the use of money. Gains from sale or exchange or retirement of bonds or other certificate of indebtedness fall within the general category of "gains derived from dealings in property" under Section 32(A)(3), while interest from bonds or other certificate of indebtedness falls within the category of "interests" under Section 32(A)(4).[204] The use of the term "gains from sale" in Section 32(B)(7)(g) shows the intent of Congress not to include interest as referred under Sections 24, 25, 27, and 28 in the exemption.[205]

Hence, the "gains" contemplated in Section 32(B)(7)(g) refers to: (1) gain realized from the trading of the bonds before their maturity date, which is the difference between the selling price of the bonds in the secondary market and the price at which the bonds were purchased by the seller; and (2) gain realized by the last holder of the bonds when the bonds are redeemed at maturity, which is the difference between the proceeds from the retirement of the bonds and the price at which such last holder acquired the bonds. For discounted instruments, like the zero-coupon bonds, the trading gain shall be the excess of the selling price over the book value or accreted value (original issue price plus accumulated discount from the time of purchase up to the time of sale) of the instruments.[206]

The Bureau of Internal Revenue rulings

The Bureau of Internal Revenue's interpretation as expressed in the three 2001 BIR Rulings is not consistent with law.[207] Its interpretation of "at

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[204] The Court of Tax Appeals, beginning in the case of *Nippon Life Insurance Company Philippines, Inc. v. Commissioner of Internal Revenue*, C.T.A. Case No. 6142, February 4, 2002 (which was affirmed by the Court of Appeals in CA-G.R. SP No. 69224, November 15, 2002), has consistently ruled that only the gain from sale (as distinguished from interest) of bonds, debentures, or other certificates of indebtedness with maturity of more than five (5) years is exempt from income tax. This ruling was reiterated in *Malayan Reinsurance Corp. (formerly Eastern General Reinsurance Corp.) v. Commissioner of Internal Revenue,* C.T.A. Case No. 6252, July 24, 2002; *Malayan Zurich Insurance Co., Inc. v. Commissioner of Internal Revenue,* C.T.A. Case No. 6251, September 30, 2002; *First Nationwide Assurance Corp. v. Commissioner of Internal Revenue,* C.T.A. Case No. 6253, October 3, 2002; *Rizal Commercial Banking Corp. v. Commissioner of Internal Revenue,* C.T.A. Case No. 6228, December 4, 2002; *Malayan Insurance Co., Inc. v. Commissioner of Internal Revenue*, C.T.A. Case No. 6243, December 16, 2002; *Tokio Marine Malayan Insurance Company, Inc. (formerly Pan Malayan Insurance Corp.) v. Commissioner of Internal Revenue*, C.T.A. Case No. 6254, January 13, 2003; *RCBC Savings Bank, Inc. v. Commissioner of Internal Revenue*, C.T.A. Case No. 6341, May 5, 2003; *Nippon Life Insurance Company of the Philippines, Inc. v. Commissioner of Internal Revenue*, C.T.A. No. 6323, July 24, 2003; *Nippon Life Insurance Company of the Philippines, Inc. v. Commissioner of Internal Revenue*, C.T.A. Case No. 6289, September 22, 2003; *Nippon Life Insurance Company of the Philippines, Inc. v. Commissioner of Internal Revenue*, C.T.A. Case No. 6348, September 12, 2003; *Tokio Marine Malayan Insurance Company, Inc. (formerly Pan Malayan Insurance Corp.) v. Commissioner of Internal Revenue*, C.T.A. Case No. 6472, December 1, 2003; *First Nationwide Assurance Corp. v. Commissioner of Internal Revenue*, C.T.A. Case No. 6473, December 22, 2003.

[205] *See Malayan Zurich Insurance Co., Inc. v. Comm.,CA*-G.R. SP No. 77070, March 28, 2005.

[206] *See* BIR Ruling No. 026-02 (2002).

[207] *See Fort Bonifacio Dev't Corp. v. Commissioner of Internal Revenue,* 617 Phil. 358, 369 (2009) [Per J. Leonardo-De Castro, En Banc]; *Executive Secretary v. Southwing Heavy Industries, Inc*., 518 Phil.

any one time" to mean at the point of origination alone is unduly restrictive.

BIR Ruling No. 370-2011 is likewise erroneous insofar as it stated (relying on the 2004 and 2005 BIR Rulings) that "all treasury bonds . . . *regardless* of the number of purchasers/lenders at the time of origination/issuance are considered deposit substitutes."[208] Being the subject of this petition, it is, thus, declared void because it completely disregarded the 20 or more lender rule added by Congress in the 1997 National Internal Revenue Code. It also created a distinction for government debt instruments as against those issued by private corporations when there was none in the law.

Tax statutes must be reasonably construed as to give effect to the whole act. Their constituent provisions must be read together, endeavoring to make every part effective, harmonious, and sensible.[209] That construction which will leave every word operative will be favored over one that leaves some word, clause, or sentence meaningless and insignificant.[210]

It may be granted that the interpretation of the Commissioner of Internal Revenue in charge of executing the 1997 National Internal Revenue Code is an authoritative construction of great weight, but the principle is not absolute and may be overcome by strong reasons to the contrary. If through a misapprehension of law an officer has issued an erroneous interpretation, the error must be corrected when the true construction is ascertained.

In *Philippine Bank of Communications v. Commissioner of Internal Revenue*,[211] this court upheld the nullification of Revenue Memorandum Circular (RMC) No. 7-85 issued by the Acting Commissioner of Internal Revenue because it was contrary to the express provision of Section 230 of the 1977 National Internal Revenue Code and, hence, "[cannot] be given weight for to do so would, in effect, amend the statute."[212] Thus:

> When the Acting Commissioner of Internal Revenue issued RMC 7-85, changing the prescriptive period of two years to ten years on claims of excess quarterly income tax payments, such circular created a clear inconsistency with the provision of Sec. 230 of 1977 NIRC. In so doing, the BIR did not simply interpret the law; rather it legislated guidelines contrary to the statute passed by Congress.

103, 129 (2006) [Per J. Ynares-Santiago, En Banc]; *Philippine Bank of Communications v. Commissioner of Internal Revenue*, 361 Phil. 916, 930 (1999) [Per J. Quisumbing, Second Division].

208 *Rollo*, p. 225.

209 *Fort Bonifacio Dev't Corp. v. Commissioner of Internal Revenue,* 617 Phil. 358, 366–367 (2009) [Per J. Leonardo-De Castro, En Banc].

210 *Philippine Health Care Providers, Inc. v. Commissioner of Internal Revenue*, 616 Phil. 387, 401–402 (2009) [Per J. Corona, Special First Division].

211 361 Phil. 916 (1999) [Per J. Quisumbing, Second Division].

212 Id. at 930.

> It bears repeating that Revenue memorandum-circulars are considered administrative rulings (in the sense of more specific and less general interpretations of tax laws) which are issued from time to time by the Commissioner of Internal Revenue. It is widely accepted that the interpretation placed upon a statute by the executive officers, whose duty is to enforce it, is entitled to great respect by the courts. Nevertheless, such interpretation is not conclusive and will be ignored if judicially found to be erroneous. Thus, courts will not countenance administrative issuances that override, instead of remaining consistent and in harmony with, the law they seek to apply and implement.[213] (Citations omitted)

This court further held that "[a] memorandum-circular of a bureau head could not operate to vest a taxpayer with a shield against judicial action [because] there are no vested rights to speak of respecting a wrong construction of the law by the administrative officials and such wrong interpretation could not place the Government in estoppel to correct or overrule the same."[214]

In *Commissioner of Internal Revenue v. Michel J. Lhuillier Pawnshop, Inc.*,[215] this court nullified Revenue Memorandum Order (RMO) No. 15-91 and RMC No. 43-91, which imposed a 5% lending investor's tax on pawnshops.[216] It was held that "the [Commissioner] cannot, in the exercise of [its interpretative] power, issue administrative rulings or circulars not consistent with the law sought to be applied. Indeed, administrative issuances must not override, supplant or modify the law, but must remain consistent with the law they intend to carry out. Only Congress can repeal or amend the law."[217]

In *Misamis Oriental Association of Coco Traders, Inc. v. Department of Finance Secretary*,[218] this court stated that the Commissioner of Internal Revenue is not bound by the ruling of his predecessors,[219] but, to the contrary, the overruling of decisions is inherent in the interpretation of laws:

> [I]n considering a legislative rule a court is free to make three inquiries: (i) whether the rule is within the delegated authority of the administrative agency; (ii) whether it is reasonable; and (iii) whether it was issued pursuant to proper procedure. But the court is not free to substitute its judgment as to the desirability or wisdom of the rule for the legislative body, by its delegation of administrative judgment, has committed those questions to administrative judgments and not to judicial judgments. In the case of an interpretative rule, the inquiry is not into the validity but into the correctness or propriety of the rule. *As a matter of power a court, when confronted with an interpretative rule, is free to (i)*

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213 Id. at 928–929.
214 Id. at 931.
215 453 Phil. 1043 (2003) [Per C.J. Davide, Jr., First Division].
216 Id. at 1059.
217 Id. at 1052.
218 G.R. No. 108524, November 10, 1994, 238 SCRA 63 [Per J. Mendoza, Second Division].
219 *BPI Family Bank v. Court of Appeals*, G.R. No. 117319, July 19, 2006, resolution.

> *give the force of law to the rule; (ii) go to the opposite extreme and substitute its judgment; or (iii) give some intermediate degree of authoritative weight to the interpretative rule.*
>
> In the case at bar, we find no reason for holding that respondent Commissioner erred in not considering copra as an "agricultural food product" within the meaning of § 103(b) of the NIRC. As the Solicitor General contends, "copra *per se* is not food, that is, it is not intended for human consumption. Simply stated, nobody eats copra for food." *That previous Commissioners considered it so, is not reason for holding that the present interpretation is wrong. The Commissioner of Internal Revenue is not bound by the ruling of his predecessors. To the contrary, the overruling of decisions is inherent in the interpretation of laws.*[220] (Emphasis supplied, citations omitted)

Tax treatment of income derived from the PEACe Bonds

The transactions executed for the sale of the PEACe Bonds are:

1. The issuance of the ₱35 billion Bonds by the Bureau of Treasury to RCBC/CODE-NGO at ₱10.2 billion; and

2. The sale and distribution by RCBC Capital (underwriter) on behalf of CODE-NGO of the PEACe Bonds to undisclosed investors at ₱11.996 billion.

It may seem that there was only one lender — RCBC on behalf of CODE-NGO — to whom the PEACe Bonds were issued at the time of origination. However, a reading of the underwriting agreement[221] and RCBC term sheet[222] reveals that the settlement dates for the sale and distribution by RCBC Capital (as underwriter for CODE-NGO) of the PEACe Bonds to various undisclosed investors at a purchase price of approximately ₱11.996 would fall on the same day, October 18, 2001, when the PEACe Bonds were supposedly issued to CODE-NGO/RCBC. In reality, therefore, the entire ₱10.2 billion borrowing received by the Bureau of Treasury in exchange for the ₱35 billion worth of PEACe Bonds was sourced directly from the undisclosed number of investors to whom RCBC Capital/CODE-NGO distributed the PEACe Bonds — all at the time of origination or issuance. At this point, however, we do not know as to how many investors the PEACe Bonds were sold to by RCBC Capital.

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220 *Misamis Oriental Association of Coco Traders, Inc. v. Department of Finance Secretary*, G.R. No. 108524, November 10, 1994, 238 SCRA 63, 69–70 [Per J. Mendoza, Second Division].

221 *Rollo*, pp. 560–574. Under the *Definitions and Interpretation*, issue date shall be on October 18, 2001; offering period shall mean the period commencing at 9:00 a.m. of October 17, 2001 and ending at 12 noon of October 17, 2001 (*Rollo,* p. 561). Under *Terms and Conditions of Application and Payment for the Bonds*, RCBC Capital shall submit to CODE-NGO a consolidated report on sales made not later than 4:00 p.m. of the last day of the offering period, and remittance of the purchase price for the bonds should be made not later than 10:00 a.m. of the issue date (*Rollo,* pp. 563–564).

222 *Rollo*, p. 576.

Should there have been a simultaneous sale to 20 or more lenders/investors, the PEACe Bonds are deemed deposit substitutes within the meaning of Section 22(Y) of the 1997 National Internal Revenue Code and RCBC Capital/CODE-NGO would have been obliged to pay the 20% final withholding tax on the interest or discount from the PEACe Bonds. Further, the obligation to withhold the 20% final tax on the corresponding interest from the PEACe Bonds would likewise be required of any lender/investor had the latter turned around and sold said PEACe Bonds, whether in whole or part, simultaneously to 20 or more lenders or investors.

We note, however, that under Section 24[223] of the 1997 National Internal Revenue Code, interest income received by individuals from long-term deposits or investments with a holding period of not less than five (5) years is exempt from the final tax.

Thus, should the PEACe Bonds be found to be within the coverage of deposit substitutes, the proper procedure was for the Bureau of Treasury to pay the face value of the PEACe Bonds to the bondholders and for the Bureau of Internal Revenue to collect the unpaid final withholding tax directly from RCBC Capital/CODE-NGO, or any lender or investor if such be the case, as the withholding agents.

The collection of tax is not barred by prescription

The three (3)-year prescriptive period under Section 203 of the 1997

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[223] Sec. 24. Income Tax Rates.

. . . .

(B) Rate of Tax on Certain Passive Income.

(1) Interests, Royalties, Prizes, and Other Winnings. - A final tax at the rate of twenty percent (20%) is hereby imposed upon the amount of interest from any currency bank deposit and yield or any other monetary benefit from deposit substitutes and from trust funds and similar arrangements; royalties, except on books, as well as other literary works and musical compositions, which shall be imposed a final tax of ten percent (10%); prizes (except prizes amounting to Ten thousand pesos (P10,000) or less which shall be subject to tax under Subsection (A) of Section 24; and other winnings (except Philippine Charity Sweepstakes and Lotto winnings), derived from sources within the Philippines: Provided, however, That interest income received by an individual taxpayer (except a nonresident individual) from a depository bank under the expanded foreign currency deposit system shall be subject to a final income tax at the rate of seven and one-half percent (7 1/2%) of such interest income: Provided, *further, That interest income from long-term deposit or investment in the form of savings, common or individual trust funds, deposit substitutes, investment management accounts and other investments evidenced by certificates in such form prescribed by the Bangko Sentral ng Pilipinas (BSP) shall be exempt from the tax imposed under this Subsection*: Provided, finally, That should the holder of the certificate pre-terminate the deposit or investment before the fifth (5th) year, a final tax shall be imposed on the entire income and shall be deducted and withheld by the depository bank from the proceeds of the long-term deposit or investment certificate based on the remaining maturity thereof:

Four (4) years to less than five (5) years – 5%;

Three (3) years to less than four (4) years – 12%; and

Less than three (3) years – 20% (Emphasis supplied)

National Internal Revenue Code to assess and collect internal revenue taxes is extended to 10 years in cases of (1) fraudulent returns; (2) false returns with intent to evade tax; and (3) failure to file a return, to be computed from the time of discovery of the falsity, fraud, or *omission*. Section 203 states:

> **SEC. 203. Period of Limitation Upon Assessment and Collection.** - *Except as provided in Section 222*, internal revenue taxes shall be assessed within three (3) years after the last day prescribed by law for the filing of the return, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period: Provided, That in a case where a return is filed beyond the period prescribed by law, the three (3)-year period shall be counted from the day the return was filed. For purposes of this Section, a return filed before the last day prescribed by law for the filing thereof shall be considered as filed on such last day. (Emphasis supplied)
>
> . . . .
>
> **SEC. 222. Exceptions as to Period of Limitation of Assessment and Collection of Taxes.**
>
> (a) In the case of a false or fraudulent return with intent to evade tax or of failure to file a return, the tax may be assessed, or a proceeding in court for the collection of such tax may be filed without assessment, at any time within ten (10) years after the discovery of the falsity, fraud or omission: Provided, That in a fraud assessment which has become final and executory, the fact of fraud shall be judicially taken cognizance of in the civil or criminal action for the collection thereof.

Thus, should it be found that RCBC Capital/CODE-NGO sold the PEACe Bonds to 20 or more lenders/investors, the Bureau of Internal Revenue may still collect the unpaid tax from RCBC Capital/CODE-NGO within 10 years after the discovery of the omission.

In view of the foregoing, there is no need to pass upon the other issues raised by petitioners and petitioners-intervenors.

Reiterative motion on the temporary restraining order

Respondents' withholding of the 20% final withholding tax on October 18, 2011 was justified

Under the Rules of Court, court orders are required to be "served upon the parties affected."[224] Moreover, service may be made personally or by

[224] RULES OF COURT, Rule 13, sec. 4.

mail.[225] And, "[p]ersonal service is complete upon actual delivery [of the order.]"[226] This court's temporary restraining order was received only on October 19, 2011, or a day after the PEACe Bonds had matured and the 20% final withholding tax on the interest income from the same was withheld.

Publication of news reports in the print and broadcast media, as well as on the internet, is not a recognized mode of service of pleadings, court orders, or processes. Moreover, the news reports[227] cited by petitioners were posted minutes before the close of office hours or late in the evening of October 18, 2011, and they did not give the exact contents of the temporary restraining order.

"[O]ne cannot be punished for violating an injunction or an order for an injunction unless it is shown that such injunction or order was served on him personally or that he had notice of the issuance or making of such injunction or order."[228]

At any rate, "[i]n case of doubt, a withholding agent may always protect himself or herself by withholding the tax due"[229] and return the amount of the tax withheld should it be finally determined that the income paid is not subject to withholding.[230] Hence, respondent Bureau of Treasury was justified in withholding the amount corresponding to the 20% final withholding tax from the proceeds of the PEACe Bonds, as it received this court's temporary restraining order only on October 19, 2011, or the day after this tax had been withheld.

Respondents' retention of the amounts withheld is a defiance of the temporary restraining order

Nonetheless, respondents' continued failure to release to petitioners the amount corresponding to the 20% final withholding tax in order that it may be placed in escrow as directed by this court constitutes a defiance of this court's temporary restraining order.[231]

The temporary restraining order is not moot. The acts sought to be enjoined are not *fait accompli.* For an act to be considered *fait accompli*, the

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225 RULES OF COURT, Rule 13, sec. 5.
226 RULES OF COURT, Rule 13, sec. 10.
227 *Rollo,* pp. 1119–1121 and 1126–1132.
228 *Spouses Lee v. Court of Appeals*, 528 Phil. 1050, 1065 (2006) [Per J. Chico-Nazario, First Division].
229 *Philippine Guaranty Co., Inc. v. Commissioner of Internal Revenue*, 121 Phil. 755, 766 (1965) [Per J. J. P. Bengzon, En Banc].
230 Id.
231 *Kibad v. Commission on Elections*, 134 Phil. 846, 850 (1968) [Per J. Fernando, En Banc].

act must have already been fully accomplished and consummated.[232] It must be irreversible, e.g., demolition of properties,[233] service of the penalty of imprisonment,[234] and hearings on cases.[235] When the act sought to be enjoined has not yet been fully satisfied, and/or is still continuing in nature,[236] the defense of *fait accompli* cannot prosper.

The temporary restraining order enjoins the entire implementation of the 2011 BIR Ruling that constitutes both the *withholding* and *remittance* of the 20% final withholding tax to the Bureau of Internal Revenue. Even though the Bureau of Treasury had already withheld the 20% final withholding tax[237] when it received the temporary restraining order, it had yet to remit the monies it withheld to the Bureau of Internal Revenue, a remittance which was due only on November 10, 2011.[238] The act enjoined by the temporary restraining order had not yet been fully satisfied and was still continuing.

Under DOF-DBM Joint Circular No. 1-2000A[239] dated July 31, 2001 which prescribes to national government agencies such as the Bureau of Treasury the procedure for the remittance of all taxes it withheld to the Bureau of Internal Revenue, a national agency shall file before the Bureau of Internal Revenue a Tax Remittance Advice (TRA) supported by withholding tax returns on or before the 10th day of the following month after the said taxes had been withheld.[240] The Bureau of Internal Revenue shall transmit an original copy of the TRA to the Bureau of Treasury,[241] which shall be the basis for recording the remittance of the tax collection.[242] The Bureau of Internal Revenue will then record the amount of taxes reflected in the TRA as tax collection in the Journal of Tax Remittance by government agencies based on its copies of the TRA.[243] Respondents did not submit any

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232 *See Benedicto v. Court of Appeals*, 510 Phil. 150, 156 (2005) [Per J. Quisumbing, First Division].

233 *Aznar Brothers Realty Company v. Court of Appeals*, 384 Phil. 95, 109–110 (2000) [Per C.J. Davide, Jr., First Division]; *Tamin v. Court of Appeals*, G.R. No. 97477, May 8, 1992, 208 SCRA 863, 875 [Per J. Gutierrez, Jr., En Banc].

234 *Quizon v. Court of Appeals,* 471 Phil. 888, 892 (2004) [Per J. Tinga, Second Division].

235 *Spouses Guerrero v. Domingo*, G.R. No. 156142, March 23, 2011, 646 SCRA 175, 179 [Per J. Leonardo-De Castro, First Division].

236 *Strategic Alliance Development Corporation v. Star Infrastructure Development Corporation*, G.R. No. 187872, April 11, 2011, 647 SCRA 545, 556 [Per J. Perez, First Division]; *Reyes-Tabujara v. Court of Appeals*, 528 Phil. 445, 458 (2006) [Per J. Chico-Nazario, First Division].

237 *Rollo*, p. 1329.

238 TAX CODE, secs. 57 and 58, as implemented by sec. 2.58(A)(2)(a) of Revenue Regulations 2-98 (as amended by Revenue Regulations 6-2001):

(2) WHEN TO FILE –

(a) For both large and non-large taxpayers, the withholding tax return, whether creditable or final (including final withholding taxes on interest from any currency bank deposit and yield or any other monetary benefit from deposit substitutes and from trust funds and similar arrangements) shall be filed and payments should be made, **within ten (10) days after the end of each month,** except for taxes withheld for the month of December of each year, which shall be filed on or before January 15 of the following year. (Emphasis and underscoring supplied)

239 Amendments to Joint Circular No. 1-2000 dated January 3, 2000 Re: Guidelines in the Remittance of All Taxes Withheld by National Government Agencies (NGAs) to the Bureau of Internal Revenue (BIR).

240 DOF-DBM Joint Circular 1-2000A, sec. 3.5.3.

241 DOF-DBM Joint Circular 1-2000A, sec. 3.3.3.

242 DOF-DBM Joint Circular 1-2000A, sec. 3.4.2.

243 DOF-DBM Joint Circular 1-2000A, sec. 3.3.4.

withholding tax return or TRA to prove that the 20% final withholding tax was indeed remitted by the Bureau of Treasury to the Bureau of Internal Revenue on October 18, 2011.

Respondent Bureau of Treasury's Journal Entry Voucher No. 11-10-10395[244] dated October 18, 2011 submitted to this court shows:

	Account Code	Debit Amount	Credit Amount
Bonds Payable-L/T, Dom-Zero Coupon T/Bonds (Peace Bonds) – 10 yr	442-360	35,000,000,000.00	
Sinking Fund-Cash (BSF)	198-001		30,033,792,203.59
Due to BIR	412-002		4,966,207,796.41
To record redemption of 10yr Zero coupon (Peace Bond) net of the 20% final withholding tax pursuant to BIR Ruling No. 378-2011, value date, October 18, 2011 per BTr letter authority and BSP Bank Statements.			

The foregoing journal entry, however, does not prove that the amount of ₱4,966,207,796.41, representing the 20% final withholding tax on the PEACe Bonds, was disbursed by it and remitted to the Bureau of Internal Revenue on October 18, 2011. The entries merely show that the monies corresponding to 20% final withholding tax was set aside for remittance to the Bureau of Internal Revenue.

We recall the November 15, 2011 resolution issued by this court directing respondents to "show cause why they failed to comply with the [TRO]; and [to] comply with the [TRO] in order that petitioners may place the corresponding funds in escrow pending resolution of the petition."[245] The 20% final withholding tax was effectively placed in *custodia legis* when this court ordered the deposit of the amount in escrow. The Bureau of Treasury could still release the money withheld to petitioners for the latter to place in escrow pursuant to this court's directive. There was no legal obstacle to the release of the 20% final withholding tax to petitioners.

Congressional appropriation is not required for the servicing of public debts in view of the automatic appropriations clause embodied in Presidential Decree Nos. 1177 and 1967.

Section 31 of Presidential Decree No. 1177 provides:

> **Section 31.** *Automatic Appropriations.* All expenditures for (a) personnel retirement premiums, government service insurance, and

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244 *Rollo*, p. 2008.
245 Id. at 1164.

> other similar fixed expenditures, (b) principal and interest on public debt, (c) national government guarantees of obligations which are drawn upon, are automatically appropriated: provided, that no obligations shall be incurred or payments made from funds thus automatically appropriated except as issued in the form of regular budgetary allotments.

Section 1 of Presidential Decree No. 1967 states:

> Section 1. There is hereby appropriated, out of any funds in the National Treasury not otherwise appropriated, such amounts as may be necessary to effect payments on foreign or domestic loans, or foreign or domestic loans whereon creditors make a call on the direct and indirect guarantee of the Republic of the Philippines, obtained by:
>
> a. the Republic of the Philippines the proceeds of which were relent to government-owned or controlled corporations and/or government financial institutions;
>
> b. government-owned or controlled corporations and/or government financial institutions the proceeds of which were relent to public or private institutions;
>
> c. government-owned or controlled corporations and/or financial institutions and guaranteed by the Republic of the Philippines;
>
> d. other public or private institutions and guaranteed by government-owned or controlled corporations and/or government financial institutions.

The amount of □35 billion that includes the monies corresponding to 20% final withholding tax is a lawful and valid obligation of the Republic under the Government Bonds. Since said obligation represents a public debt, the release of the monies requires no legislative appropriation.

Section 2 of Republic Act No. 245 likewise provides that the money to be used for the payment of Government Bonds may be lawfully taken from the continuing appropriation out of any monies in the National Treasury and is not required to be the subject of another appropriation legislation:

> SEC. 2. *The Secretary of Finance shall cause to be paid out of any moneys in the National Treasury not otherwise appropriated, or from any sinking funds provided for the purpose by law, any interest falling due, or accruing, on any portion of the public debt authorized by law. He shall also cause to be paid out of any such money, or from any such sinking funds the principal amount of any obligations which have matured, or which have been called for redemption or for which redemption has been demanded in accordance with terms prescribed by him prior to date of issue . . .* In the case of interest-bearing obligations, he shall pay not less

> than their face value; in the case of obligations issued at a discount he shall pay the face value at maturity; or if redeemed prior to maturity, such portion of the face value as is prescribed by the terms and conditions under which such obligations were originally issued. There are hereby appropriated as a continuing appropriation out of any moneys in the National Treasury not otherwise appropriated, such sums as may be necessary from time to time to carry out the provisions of this section. The Secretary of Finance shall transmit to Congress during the first month of each regular session a detailed statement of all expenditures made under this section during the calendar year immediately preceding.

Thus, DOF Department Order No. 141-95, as amended, states that payment for Treasury bills and bonds shall be made through the National Treasury's account with the Bangko Sentral ng Pilipinas, to wit:

> **Section 38.** *Demand Deposit Account.* – The Treasurer of the Philippines maintains a Demand Deposit Account with the Bangko Sentral ng Pilipinas to which all proceeds from the sale of Treasury Bills and Bonds under R.A. No. 245, as amended, shall be credited and all payments for redemption of Treasury Bills and Bonds shall be charged.

Regarding these legislative enactments ordaining an automatic appropriations provision for debt servicing, this court has held:

> Congress . . . deliberates or acts on the budget proposals of the President, and Congress in the exercise of its own judgment and wisdom formulates an appropriation act precisely following the process established by the Constitution, which specifies that no money may be paid from the Treasury except in accordance with an appropriation made by law.
>
> Debt service is not included in the General Appropriation Act, since authorization therefor already exists under RA Nos. 4860 and 245, as amended, and PD 1967. Precisely in the light of this subsisting authorization as embodied in said Republic Acts and PD for debt service, Congress does not concern itself with details for implementation by the Executive, but largely with annual levels and approval thereof upon due deliberations as part of the whole obligation program for the year. Upon such approval, Congress has spoken and cannot be said to have delegated its wisdom to the Executive, on whose part lies the implementation or execution of the legislative wisdom.[246] (Citation omitted)

Respondent Bureau of Treasury had the duty to obey the temporary restraining order issued by this court, which remained in full force and effect, until set aside, vacated, or modified. Its conduct finds no justification

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[246] *Spouses Constantino, Jr. v. Cuisia*, 509 Phil. 486, 513–514 [Per J. Tinga, En Banc].

and is reprehensible.[247]

WHEREFORE, the petition for review and petitions-in-intervention are **GRANTED**. BIR Ruling Nos. 370-2011 and DA 378-2011 are **NULLIFIED**.

Furthermore, respondent Bureau of Treasury is **REPRIMANDED** for its continued retention of the amount corresponding to the 20% final withholding tax despite this court's directive in the temporary restraining order and in the resolution dated November 15, 2011 to deliver the amounts to the banks to be placed in escrow pending resolution of this case.

Respondent Bureau of Treasury is hereby **ORDERED** to immediately release and pay to the bondholders the amount corresponding to the 20% final withholding tax that it withheld on October 18, 2011.

MARVIC M.V.F. LEONEN
Associate Justice

WE CONCUR:

MARIA LOURDES P. A. SERENO
Chief Justice

ANTONIO T. CARPIO
Associate Justice

PRESBITERO J. VELASCO, JR.
Associate Justice

TERESITA J. LEONARDO-DE CASTRO
Associate Justice

(On leave)
ARTURO D. BRION
Associate Justice

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[247] *Kibad v. Commission on Elections*, 134 Phil. 846, 849–850 (1968) [Per J. Fernando, En Banc]; *Commissioner of Immigration v. Cloribel*, 127 Phil. 716 (1967) [Per Curiam, En Banc].

DIOSDADO M. PERALTA
Associate Justice

LUCAS P. BERSAMIN
Associate Justice

MARIANO C. DEL CASTILLO
Associate Justice

MARTIN S. VILLARAMA, JR.
Associate Justice

JOSE PORTUGAL PEREZ
Associate Justice

JOSE CATRAL MENDOZA
Associate Justice

BIENVENIDO L. REYES
Associate Justice

ESTELA M. PERLAS-BERNABE
Associate Justice

FRANCIS H. JARDELEZA
Associate Justice

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C E R T I F I C A T I O N

I certify that the conclusions in the above Decision had been reached in consultation before the case was assigned to the writer of the opinion of the court.

MARIA LOURDES P. A. SERENO
Chief Justice