

REPUBLIC OF THE PHILIPPINES
DEPARTMENT OF FINANCE
BUREAU OF INTERNAL REVENUE

Date: November 07, 2012

REVENUE REGULATIONS NO. 14-2012

Subject: Proper Tax Treatment of Interest Income Earnings on Financial Instruments and Other Related Transactions.

To: All Internal Revenue Officials and Employees Concerned

SECTION 1. Scope. –

Pursuant to the provisions of Sections 57, 244 and 245 of the National Internal Revenue Code (NIRC) of 1997, as amended, and in light of the resolution contained in the PEACe Bond Ruling, these Regulations are hereby promulgated to properly implement the income taxation of interest income earnings on financial instruments and similar transactions based on existing laws and regulations and to rationalize the tax exemptions of interest income derived therefrom.

SECTION 2. Tax Treatment of Interest Income Derived from Government Debt Instruments and Securities. –

“*Deposit Substitutes*”, as defined in Section 22(Y) of the NIRC of 1997, as amended, means 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 re-lending or purchasing of receivables and other obligations, or financing their own needs or the needs of their agent or dealer.

“*Public*”, is defined as borrowing from twenty (20) or more individual or corporate lenders at any one time.

Consistent with the foregoing definitions, the tax treatment of interest income derived from government debt instruments and securities is as follows:

1. Government Debt Instruments and Securities, including Bureau of Treasury (BTr) issued instruments and securities such as Treasury bonds (T-bonds), Treasury bills (T-bills) and Treasury notes, shall be considered as deposit substitutes irrespective of the number of lenders at the time of

origination if such debt instruments and securities are to be traded or exchanged in the secondary market;

2. Interest income derived therefrom is subject to Final Withholding Tax (FWT) at the rate of twenty percent (20%) pursuant to Sections 24(B)(1), 25(A)(2), 27(D)(1) and 28(A)(7)(a) or twenty five percent (25%) pursuant to Section 25(B) or thirty percent (30%) pursuant to Section 28(B)(1) of the NIRC of 1997, as amended, payable upon original issuance of the deposit substitutes;
3. The original issuance of these debt instruments is subject to documentary stamp tax (DST) pursuant to Section 179 of the NIRC of 1997, as amended;
4. The mere issuance of government debt instruments and securities is deemed as falling within the coverage of 'deposit substitutes' irrespective of the number of lenders at the time of origination, and therefore interest income derived therefrom shall be subject to the applicable final withholding tax rate imposed on deposit substitutes as prescribed under the NIRC of 1997, as amended.

SECTION 3. Tax Treatment of Interest Income Derived from Long-Term Deposits or Investment Certificates. –

"Long-term Deposit or Investment Certificate", as defined in Section 22(FF) of the NIRC of 1997, as amended, refers to certificate of time deposit or investment in the form of savings, common or individual trust funds, deposit substitutes, investment management accounts and other investments with a maturity period of not less than five (5) years, the form of which shall be prescribed by the Bangko Sentral ng Pilipinas (BSP) and issued by banks only (not by non-bank financial intermediaries and finance companies) to individuals in denominations of Ten thousand pesos (P10,000) and other denominations as may be prescribed by the BSP.

Consistent with the foregoing definition, the tax treatment of interest income derived from Long-Term Deposits or Investment Certificates is as follows:

1. 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 income tax under Section 24(B)(1) and 25(A)(2) of the NIRC of 1997, as amended, provided that the following characteristics/ conditions are present:

- a. the depositor or investor is an individual citizen (resident or nonresident), a resident alien or a nonresident alien engaged in trade or business in the Philippines;
 - b. the long-term deposits or investment certificates should be under the name of the individual and not under the name of the corporation or the bank or the trust department/unit of the bank;
 - c. the long-term deposits or investments must be 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);
 - d. the long-term deposits or investments must be issued by banks only and not by other financial institutions;
 - e. the long-term deposits or investments must have a maturity period of not less than five (5) years;
 - f. the long-term deposits or investments must be in denominations of Ten thousand pesos (P10,000) and other denominations as may be prescribed by the BSP;
 - g. the long-term deposits or investments should not be terminated by the investor before the fifth (5th) year, otherwise they shall be subjected to the graduated rates of 5%, 12% or 20% on interest income earnings; and
 - h. except those specifically exempted by law or regulations, any other income such as gains from trading, foreign exchange gain shall not be covered by income tax exemption.
2. Absent any of the characteristics/conditions enumerated in Section 4(1) of these Regulations, interest income from long-term deposit or investment shall be subject to a Final Withholding Tax (FWT) at the rate of twenty percent (20%) pursuant to Sections 24(B)(1), 25(A)(2), 27(D)(1) and 28(A)(7)(a) of the NIRC of 1997, as amended.
3. Interest income from long-term deposit or investment that is pre-terminated by the depositor or investor before the fifth (5th) year shall be subject to the following graduated rates of Final Withholding Tax (FWT) 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 as follows:

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%.

Example No. 1 –

An instrument with a maturity period of 10 years was held by Mr. X (a resident citizen) for 2 years and was transferred to Mr. Y (a resident alien), who, in turn, held it for 8 years. The FWT due are as follows:

Mr. X	2 years	20% FWT
Mr. Y	8 years	Exempt

Example No. 2 –

An instrument with maturity period of 10 years was held by Mr. X (a nonresident citizen) for 3 years and transferred it to Mr. Y (a resident alien). Mr. Y held it for 2 years before subsequently transferring it to Mr. Z (a resident citizen), who held it until the day of maturity or for 5 years. The FWT due are as follows:

Mr. X	3 years	12% FWT
Mr. Y	2 years	20% FWT
Mr. Z	5 years	Exempt

Example No. 3 –

An instrument with maturity period of 10 years held by Mr. X (a nonresident alien engaged in trade or business in the Philippines) for 3 years and transferred it to Mr. Y (a resident citizen). Mr. Y held it for 2 years before subsequently transferring it to Mr. Z (a resident alien), who pre-terminated it after 4 years. The FWT due are as follows:

Mr. X	3 years	12% FWT
Mr. Y	2 years	20% FWT
Mr. Z	4 years	5% FWT

4. Interest income from long-term deposit or investment shall be subject to a Final Withholding Tax (FWT) at the rate of twenty five percent (25%) if received by a nonresident alien not engaged in trade or business in the Philippines pursuant to Section 25(B) of the NIRC of 1997, as amended;
5. Interest income from long-term deposit or investment shall be subject to a Final Withholding Tax (FWT) at the rate of thirty percent (30%) if received

by a nonresident foreign corporation pursuant to Section 28(B)(1) of the NIRC of 1997, as amended.

6. Interest income from long-term deposit or investment shall be subject to regular income tax at the rate of thirty percent (30%) if received by a domestic corporation and resident foreign corporation pursuant to Sections 27(A) and 28(A)(1) of the NIRC of 1997, as amended.

SECTION 4. Tax Treatment of Interest Income Derived from Currency Bank Deposit and Yield or any other Monetary Benefit from Deposit Substitutes and from Trust Funds and Similar Arrangements. –

Consistent with the provisions of Sections 24(B)(1), 25(A)(2), 25(B), 27(D)(1), 28(A)(7)(a), 28(B)(1) and 28(B)(5)(a) of the NIRC of 1997, as amended, the tax treatment of interest income derived from currency bank deposit and yield or any other monetary benefit from deposit substitutes and from trust funds and similar arrangements derived from sources within the Philippines, is as follows:

1. Subject to a Final Withholding Tax (FWT) of twenty percent (20%) if the interest income is received by:
 - a. citizens;
 - b. resident aliens;
 - c. nonresident aliens engaged in trade or business in the Philippines;
 - d. domestic corporations; and
 - e. resident foreign corporation
2. Subject to a Final Withholding Tax (FWT) at the rate of twenty five percent (25%) if the interest income is received by nonresident aliens not engaged in trade or business in the Philippines;
3. Subject to Final Withholding Tax (FWT) at the rate of thirty percent (30%) if received by a nonresident foreign corporation, unless the interest income is from foreign loans contracted on or after August 1, 1986, in which case, it is subject to a Final Withholding Tax (FWT) of twenty percent (20%).

SECTION 5. Tax Treatment of Interest Income Derived from a Depository Bank under the Expanded Foreign Currency Deposit System. –

Consistent with the provisions of Sections 24(B)(1), 27(D)(1), 27(D)(3), 28(A)(7)(a), and 28(A)(7)(b) of the NIRC of 1997, as amended, the tax treatment of interest income derived from a depository bank under the Expanded Foreign Currency Deposit System, is as follows:

1. Subject to a Final Withholding Tax (FWT) of seven and one-half percent (7.5%) if the interest income is received by:
 - a. citizens;
 - b. resident aliens;
 - c. domestic corporations; and
 - d. resident foreign corporation
2. Any income of nonresidents, whether individuals or corporations, from transactions with depository banks under the expanded system shall be exempt from income tax;
3. If a bank account is jointly in the name of a non-resident citizen such as an overseas contract worker, or a Filipino seaman, and his/her spouse or dependent who is a resident in the Philippines, fifty percent (50%) of the interest income from such bank deposit shall be treated as exempt while the other fifty percent (50%) shall be subject to a Final Withholding Tax (FWT) of seven and one-half percent (7.5%);
4. Income derived by a depository bank under the expanded foreign currency deposit system from foreign currency transactions with nonresidents, offshore banking units in the Philippines, local commercial banks including branches of foreign banks that may be authorized by the Bangko Sentral ng Pilipinas (BSP) to transact business with foreign currency deposit system units and other depository banks under the expanded foreign currency deposit system shall be exempt from all taxes, except net income from such transactions as may be specified by the Secretary of Finance, upon recommendation by the Monetary Board to be subject to the regular income tax payable by banks;
5. Interest income from foreign currency loans granted by such depository banks under said expanded system to residents other than offshore banking units in the Philippines or other depository banks under the expanded system shall be subject to a final tax at the rate of ten percent (10%).

SECTION 6. Tax Treatment of Interest Income Derived from Offshore Banking Units. –

Consistent with the provision of Section 28(A)(4) of the NIRC of 1997, as amended, the tax treatment of interest income derived from offshore banking units are as follows:

1. Income derived by offshore banking units authorized by the Bangko Sentral ng Pilipinas (BSP), from foreign currency transactions with nonresidents, other offshore banking units, local commercial banks, including branches of

- foreign banks that may be authorized by the Bangko Sentral ng Pilipinas (BSP) to transact business with offshore banking units shall be exempt from all taxes except net income from such transactions as may be specified by the Secretary of Finance, upon recommendation of the Monetary Board which shall be subject to the regular income tax payable by banks;
2. Interest income derived from foreign currency loans granted to residents other than offshore banking units or local commercial banks, including local branches of foreign banks that may be authorized by the BSP to transact business with offshore banking units, shall be subject only to a Final Withholding Tax (FWT) at the rate of ten percent (10%);
 3. Any income of nonresidents, whether individuals or corporations, from transactions with said offshore banking units shall be exempt from income tax.

SECTION 7. Tax Treatment of Interest Income Derived from All Other Instruments. –

Unless otherwise provided by law or regulations, interest income derived from any other debt instruments not within the coverage of 'deposit substitutes'; and these Regulations shall be subject to a Creditable Withholding Tax (CWT) at the rate of twenty percent (20%). For this purpose, the income payor is required to withhold and remit the said tax to the Bureau of Internal Revenue in accordance with Sections 2.57.3, 2.57.4 and 2.58 of Revenue Regulations No. 2-98, as amended.

For this purpose, Section 2.57.2 of Revenue Regulations No. 2-98, as amended, is hereby further amended, to read as follows:

SECTION 2.57.2. Income Payment Subject to Creditable Withholding Tax and Rates Prescribed Thereon. – Except as herein otherwise provided, there shall be withheld a creditable income tax at the rates herein specified for each class of payee from the following items of income payments to persons residing in the Philippines:

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(Y) Interest income derived from any other debt instruments not within the coverage of 'deposit substitutes' and Revenue Regulations No. - 2012, unless otherwise provided by law or regulations --- Twenty Percent (20%).

SECTION 8. The “19-Lender Rule”. –

In order for an instrument to qualify as a “deposit substitute” pursuant to Section 22 (Y) of the NIRC of 1997, as amended, the borrowing must be made from twenty (20) or more individual or corporate lenders at any one time. Corollarily, the mere flotation of a debt instrument is not considered to be a “public” borrowing and is not deemed a “deposit substitute” if there are only nineteen (19) or less individual or corporate lenders at any one time.

However, any person holding any interest, whether legal or beneficial, on a debt instrument or holding thereof either by assignment or participation, with or without recourse, shall be considered as lender and thus, be counted in applying the 19-lender rule.

SECTION 9. Documentary Stamp Tax. – The original issuance of debt instruments shall be subject to Documentary Stamp Tax in accordance with Section 179 of the NIRC of 1997, as amended. Thus, on every original issue of debt instruments, there shall be collected a documentary stamp tax of one peso (P1.00) on each two hundred pesos (P200), or fractional part thereof, of the issue price of any such debt instrument. However, any assignment or re-assignment of said debt instruments shall be subject to the same documentary stamp tax mentioned above pursuant to Section 198 of the NIRC of 1997.

SECTION 10. Repealing Clause. —

All existing rules and regulations and other issuances or parts thereof which are inconsistent with the provisions of these Regulations are hereby modified, amended or revoked accordingly.

SECTION 11. Effectivity Clause. —

These Regulations shall take effect after fifteen (15) days following complete publication in a newspaper of general circulation in the Philippines.

(Original Signed)
CESAR V. PURISIMA
Secretary of Finance

Recommending approval:

(Original Signed)
KIM S. JACINTO-HENARES
Commissioner of Internal Revenue