

**[BIR REVENUE REGULATIONS NO. 13-2000,
November 20, 2000]**

**IMPLEMENTING SECTION 34(B) OF THE TAX CODE OF 1997 ON
THE REQUIREMENTS FOR DEDUCTIBILITY OF INTEREST
EXPENSE FROM THE GROSS INCOME OF A TAXPAYER**

SECTION 1. Scope - Pursuant to the provisions of Section 244 of the Tax Code of 1997, these Regulations are hereby promulgated to implement the provisions of Section 34(B) of the same Code on the requirements for deductibility of interest expense from the gross income of a corporation or an individual engaged in trade, business or in the practice of profession.

SEC. 2. Definition of Terms - For purposes of these Regulations, the following words and phrases shall have the following meaning, viz:

(a) *Interest* - shall refer to the payment for the use or forbearance or detention of money, regardless of the name it is called or denominated. It includes the amount paid for the borrower's use of money during the term of the loan, as well as for his detention of money after the due date for its repayment.

(b) *Taxpayer*- shall refer to a person, whether natural or juridical, engaged in trade, business or in the exercise of profession, except one earning compensation income arising from personal services rendered under an employer-employee relationship.

SEC. 3. Requisites for Deductibility of interest Expense - In general, subject to certain limitations, the following are the requisites for the deductibility of interest expense from gross income, viz:

- (a) There must be an indebtedness;
- (b) There should be an interest expense paid or incurred upon such indebtedness;
- (c) The indebtedness must be that of the taxpayer;
- (d) The indebtedness must be connected with the taxpayer's trade, business or exercise of profession;
- (e) The interest expense must have been paid or incurred during the taxable year;
- (f) The interest expense must have been stipulated in writing;

(g) The interest must be legally due;

(h) The interest payment arrangement must not be between related taxpayers as mandated in Sec. 34(B)(2)(b), in relation to Sec. 36(B), both of the Tax Code of 1997;

(i) The interest must not be incurred to finance petroleum operations; and

(j) In case of interest incurred to acquire property used in trade, business or exercise of profession, the same was not treated as a capital expenditure.

SEC. 4. Rules on the Deducibility of Interest Expense

(a) *General Rule* - In general, the amount of interest expense paid or incurred within a taxable year on indebtedness in connection with the taxpayer's trade, business or exercise of profession shall be allowed as a deduction from the taxpayer's gross income.

(b) *Limitation* - The amount of interest expense paid or incurred by a taxpayer in connection with his trade, business or exercise of a profession from an existing indebtedness shall be reduced by an amount equal to the following percentages of the interest income earned which had been subjected to final withholding tax depending on the year when the interest income was earned, viz:

Forty-one percent (41%) beginning January 1, 1998;
Thirty-nine percent (39%) beginning January 1, 1999; and
Thirty-eight percent (38%) beginning January 1, 2000 and thereafter.

This limitation shall apply regardless of whether or not a tax arbitrage scheme was entered into by the taxpayer or regardless of the date when the interest bearing loan and the date when the investment was made for as long as, during the taxable year, there is an interest expense incurred on one side and an interest income earned on the other side, which interest income had been subjected to final withholding tax. This rule shall be observed irrespective of the currency the loan was contracted and/or in whatever currency the investments or deposits were made.

Illustration: Supposing on January 15, 1998, Company A, Who has a deposit account with BCD Bank, obtained a loan from XYZ Financing Corporation in connection with the operation of its business. Assume that Company A's net income for the year 1998 before the deduction of the interest expense amounted to P1,000,000. For the year 1998, the interest income it derived from the said deposit with BCD Bank amounted to P180,000 on which a final tax of P36,000 had been withheld. Its interest expense on the loan obtained from XYZ Financing Corporation during the same year amounted to P150,000.

Under this illustration, the deductible interest expense, the taxable income and the income tax due of Company A shall be computed as follows: