

## Chapter 1. Succession and Transfer Taxes

**Succession** - is a mode of acquisition by virtue of which the property, rights and obligations to the extent of the value of the inheritance, of a person are transmitted through his death to another or others either by his will or by operation of law. (Art. 774 NCC)

The rights to the succession are transmitted from the moment of the death of the decedent. (Art. 777)

### Requisites:

1. Death of the predecessor;
2. Existence and capacity of the successor;
3. Provision of the law or provision of a will granting the right to succession;
4. Acceptance by the successor.

**Transfer Taxes** - are taxes imposed upon the gratuitous disposition of private properties or rights.

Gratuitous transfer - is the one that neither imposes burden nor requires consideration from transferee or recipient.

Two types of gratuitous transfer:

1. Donation mortis causa - is the transfer which takes effect at the time of death of the donor or transferor. This is subject to estate tax.
2. Donation inter vivos - is the transfer which takes effect during the lifetime of both the donor and the donee. This is subject to donor's tax.

Onerous transfer - is the one where the transferee gives consideration in return for the property or rights received. (e.g. sale)

### Nature of Transfer Taxes

A transfer tax is imposed on the privilege of the transferor to gratuitously transfer property or rights which takes effect at the date of death of the transferor or during the lifetime of the donor and the donee. Although the amount of tax is based on the net value of the property being transferred, it shall not be construed as a property tax. It is classified as an "excise tax" imposed on the act of passing the ownership of property and not on the property itself.

**Applicable Law:** estate taxation is governed by the law in force at the time of death of the decedent. (Sec. 3, RR No. 2-2003)

### Kinds of Succession:

1. Testamentary or testate - results from the designation of an heir, made in a will executed in the form prescribed by law.
2. Intestate or legal - effected by operations of law since the decedent did not execute a will or if the last will and testament executed by him is void.
3. Mixed - effected partly by will and by operation of law.

### Elements of Succession:

1. Decedent - is a general term applied to the person whose property is transmitted through succession whether or not he left a will. If he left a will, he is called a testator. Every TESTATOR is a decedent, but not all decedents are testators.

Executor - a person designated in the last will and testament to carry out the provisions of the decedent's will.

Administrator is a person appointed by the court and performs the same duty, in lieu of an executor, if the latter refused to accept the appointment, failed to qualify under the law or the will did not appoint one.

2. Inheritance - includes all the property, rights and obligations of a person which are not extinguished by death and all which have accrued thereto since the opening of succession.

Purely personal rights - are extinguished by the death of the decedent and do not form part of the inheritance. (e.g. membership in the Philippine Institute of Certified Public Accountants)

3. Successors - an heir or successor is a person called to the succession either by the provision of a will or by operation of law.

Successors classified as follows:

- a. Compulsory heirs - those who succeed by force of law to some portion of the inheritance, in an amount predetermined by law, known as the legitime. They cannot be deprived by the testator except by disinheritance properly effected.
- b. Voluntary heirs - those instituted by the testator in his will to succeed to the inheritance of the portion thereof of which the testator can freely dispose.
- c. Legal or intestate heirs - those who succeed to the estate of the decedent by operation of law.

Devises are persons to whom gifts of real properties are given by virtue of a will, while legatees are persons whom gifts of personal property are given also by virtue of a will.

Heir	Devisee or Legatee
An heir succeeds to whole or fractional part of the estate (universal)	A devisee or legatee succeeds to a definite, specific and individualized properties (particular)
An heir succeeds to either by will or law	A devisee or legatee succeeds ONLY by a virtue of a will
In case of preterition (Art. 854), institution of heirs is annulled.	Not affected by preterition unless there is impairment of legitime

## Testamentary Succession

**Will** - is an act whereby a person is permitted, with the formalities prescribed by law, to control to a certain degree the disposition of his estate, to take effect after his death. (Art. 783)

To a certain degree - the testator cannot deprive the compulsory heirs of their legitimes. The power to dispose is absolute if there is NO compulsory heirs. Otherwise, it is limited to a certain degree. That is why the will can only cover the disposable (free) portion of the estate.

### Characteristics of a Will:

1. It is a purely personal act (Art. 784) - it cannot be left in whole or in part of the discretion of a third person, or accomplished through the instrumentality of an agent or attorney. What cannot be delegated is the disposing power, but the physical act of making the will can be delegated except for holographic wills.
2. Free act - without fraud, violence, deceit, duress or intimidation. It is voluntary.
3. Dispositive of property - it must be directed towards disposition of the estate otherwise it will be useless. Unless it was made:
  - a. To recognize an illegitimate child;
  - b. To disinherit a compulsory heir; or
  - c. To appoint an executor.
4. Essentially revocable - ambulatory (meaning capable of being altered); it is not fixed, can be taken back while the testator is still alive. The will becomes irrevocable only upon death of the testator.
5. Formally executed - it must conform with the formal requirements of law.
6. Testamentary capacity of the testator - testamentification activa is the capacity to make a will. Persons under eighteen (18) years of age cannot make a will. It is also essential that the testator be of sound mind at the time of execution.

Sound mind means realization of the following:

- a. Nature of the estate - the testator should at least have a fair accurate idea what his properties are, it is not necessary that he know the properties in detail.
  - b. Proper objects of his bounty - know his immediate relatives.
  - c. Character of the testamentary act - know the essence of making a will. He is expected to know that he is making a document disposing of his property gratuitously and such disposition is to take effect upon his death.
7. Unilateral act - does not involve an exchange of values or depend on simultaneous offer and acceptance.
  8. Mortis causa - takes effect upon the testator's death.
  9. Statutory - granted by civil law and not by the constitution.
  10. Animus Testandi - intent to dispose. There must be a real intent to dispose of the property upon death.
  11. Individual - one person alone, joint wills are prohibited under Art. 818.

## Kinds of Wills

Every will must be in writing an executed in a language or dialect known to the testator.

Oral wills or non-cupative wills, which are done by the testator in contemplation of death, are not allowed under the Civil Code. This is allowed among Muslims only.

**Notarial or Ordinary or Attested Will** - is one which is executed in accordance with the formalities prescribed by the Art. 804 to 808 of the Civil Code.

Special requirements for Notarial or Attested Wills (Art. 805-809):

1. It must be subscribed at the end thereof by the testator himself or by the testator's name written by some other person in his presence, and by his express direction.

Subscription may be done by writing his name or affixing his thumbmark (Matias vs. Salud). A thumbmark, according to the case, is a valid way to sign a will. It is less possible to forge and maybe done by the testator whether or not he is literate. However, there may also be the danger of falsification by affixing a thumbmark of a dead person (Balane).

Cross or any other symbols are not valid ways of signing since this can easily be falsified (Garcia vs. de la Cuesta). Except: if this is the normal way of signing of the testator (Balane).

Writing of the testator's name should be by hand otherwise it will not be valid (Barut vs. Cabacungan) even if the agent writes his name on top of the typewritten name of the testator (Balonan vs. Abellana).

2. It must attested and subscribed by three or more credible witnesses in presence of the testator and of one another.
3. The testator or the person requested by him to write his name and instrumental witnesses of the will, shall also sign, each and every page thereof, except the last (already signed at the bottom), and all the pages shall be numbered correlatively.
4. The attestation clause shall state the number of pages used upon which the will is written, and the fact that the testator signed the will and every page thereof, or caused some other person to write his name, under his express direction, in the presence of the witnesses, and that the latter witnessed and signed the will and all the pages thereof in the presence of the testator and of one another.

Attestation is part of the will itself but is a formal requirement to make a will valid. Placed at the bottom in order to prevent additions. This is required only for notarial wills and not in holographic wills since there are no witnesses in a holographic will and an attestation is an act by the witnesses.

**Holographic Will** - must be entirely written, dated, and signed by the hand of the testator himself. It is subject to

no other form, and may be made in or out of the Philippines, and need not be witnessed. (Art. 810)

In the probate of a holographic will, it shall be necessary that at least one witness who knows the handwriting and signature of the testator explicitly declare that the will and the signature are in the handwriting of the testator. If the will is contested, at least three of such witnesses shall be required.

Probate - is the process of proving in court that the will of a person who has died is valid.

Codicil - is a supplement or addition to a will, made after the execution of a will and annexed to be taken a part thereof, by which disposition made in the original will is explained, added to, or altered. If it makes independent disposition, it is considered another will.

Form of codicil: need not conform with the will itself. It is sufficient that it complies with the form of wills (either holographic or notarial).

### **Revocation of Wills and Testamentary Dispositions**

A will may be revoked by the testator at any time before his death. Any waiver or restriction of this right is void (Art. 828). One of the characteristics of a will is that it is ambulatory and is revocable.

A revocation done outside the Philippines, by a person who does not have his domicile in this country, is valid when it is done according to the law of the place where the will was made, or according to the law of the place where the will was made, or according to the law of the place in which the testator had his domicile at the time; and if the revocation takes place in this country, when it is in accordance with the provisions of this Code (Art. 829)

### **Ways of Revoking a Will:**

1. Implication of law
  - a. Unworthiness to succeed
  - b. Transformation of the property by the testator - devise or legacy
  - c. Legal separation
  - d. Preterition annuls the institution of heirs
2. Subsequent instrument, Will or Codicil
3. Physical destruction (limited to burning, tearing, canceling, or obliterating the will)

Requisites of revoking a will through a subsequent document:

- a. Capacity to revoke
- b. Revoking instrument must be valid
- c. Revoking clause whether express or implied
- d. Revoking will must be probated

Elements of Physical Destruction:\*

- a. Corpus - act of destruction. Need not be total destruction as long as there is evidence on the face of the will which shows the act to revoke.
- b. Animus - intent and capacity to revoke.

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Transfer and Business Taxation (TAX 2) based on the book of Enrico Tabag and Earl Garcia and the notes of Cesar Nickolai Soriano

\*Both elements must concur. If burned accidentally, there no animus and thus no revocation. However, there is no will to probate. Unless, a copy can be secured and presented. Otherwise, there would be no will and legal succession will occur.

**Institution of Heirs** - is an act by virtue of which a testator designated in his will the person who are to succeed him in his property and transmissible rights and obligations. (Art. 840)

Identity of the heir is what's important and not the name. Although, as a general rule, the heir should be designated by name and surname.

Errors in the name of the heir is immaterial as long as he can still be identified.

Ambiguity as to identity shall be resolved by evidence. If an ambiguity still exists, none of them may inherit.

The following will not invalidate a will:

1. Absence of any institution to heirs;
2. If the will does not cover the whole estate;
3. Non-acceptance of the inheritance;
4. Incapacity to succeed.

**Preterition** - means an omission of one, or some, or all of the compulsory heirs in the direct line, whether living at the time of the execution of the will or born after the death of the testator, shall annul the institution of heir; but the devisees and legatees shall be valid as they are not inofficious.

**Legitimate** - is that part of the testator's property which he cannot dispose of because the law has reserved it for certain heirs who are, therefore, called compulsory heirs.

### **The following are compulsory heirs:**

1. Legitimate children and descendants, with respect to their legitimate parents and ascendants;
2. In default of the foregoing, legitimate parents and ascendants, with respect to their legitimate children and ascendants;
3. The widow or widower;
4. Illegitimate children.

### **Compulsory heirs are classified as follows:**

1. Primary - legitimate children and/or descendants;
2. Secondary - legitimate parents and/or ascendants; illegitimate parents;
3. Concurring - illegitimate children and/or descendants and surviving spouse.

The existence of primary heirs exclude the secondary. Such that, if a testator dies with legitimate children/descendants, the legitimate parents are excluded as compulsory heirs.

### **Legitimes:**

1. General rule - the basic quota of 1/2 that is given to one heir or one group of heirs. This general rule admits only three exceptions:
  - a. Surviving spouse and illegitimate children:
    - i. Surviving spouse - 1/3
    - ii. Illegitimate Children - 1/3
    - iii. Free portion - 1/3
  - b. Surviving spouse is sole heir in a marriage and the testator dies within 3 months from the time of marriage:
    - i. Surviving spouse - 1/3 if sole heir
    - ii. Surviving spouse of married for more than 5 years at the time of death - 1/2
    - iii. Free portion - 2/3 or 1/2, as the case may be.
  - c. Surviving spouse and illegitimate parents:
    - i. Surviving spouse - 1/4
    - ii. Illegitimate parents - 1/4
    - iii. Free portion - 2/4

**With legitimate child(ren):**

2. Only legitimate children - 1/2 of the estate divided equally amongst them;
3. Legitimate children and surviving spouse:
  - a. LC - 1/2
  - b. SS - a share equal to that of one child
4. Legitimate children and illegitimate children:
  - a. LC - 1/2
  - b. IC - 1/2 of the share of a LC (Art. 176, Family Code)
5. Legitimate children, illegitimate children, and SS:
  - a. LC - 1/2
  - b. IC - 1/2 of the share of a LC
  - c. SS - share equal to that of one LC
6. One legitimate child and surviving spouse:
  - a. LC - 1/2
  - b. SS - 1/4 (Art. 892, par. 1)
7. One legitimate child, illegitimate children, and SS:
  - a. LC - 1/2
  - b. SS - 1/4
  - c. IC - 1/2 share of the LC (e.i. 1/4)

**No legitimate child; with legitimate parents:**

8. Legitimate parents alone: 1/2 of the estate
9. Legitimate parents and illegitimate children:
  - a. LP - 1/2
  - b. IC - 1/4
10. Legitimate parents and SS:
  - a. LP - 1/2
  - b. SS - 1/4
11. Legitimate parents, illegitimate children and SS:
  - a. LP - 1/2
  - b. IC - 1/4
  - c. SS - 1/8 (Art. 899)

**No legitimate child and no legitimate parents:**

12. SS - 1/2 or 1/3
13. Illegitimate children alone - 1/2
14. Illegitimate parents alone - 1/2
15. Illegitimate parents and SS - 1/4 to SS and 1/4 to IP

**Disinheritance**

A compulsory heir may, in consequence of disinheritance, be deprived of his legitime, for causes expressly stated by law.

**Requisites:**

1. It must be made in a will;
2. It must be for a cause specified by law;
3. The will must specify the cause;
4. It must be unconditional;
5. It must be total;
6. The cause must be true;
7. If the truth of the cause is denied, it must be proved by the proponent.

**Causes for the disinheritance of children and descendants, legitimate as well as illegitimate:**

1. When a child or descendant has been found guilty of an attempt against the life of the testator, his or her spouse, descendants, or ascendants;
2. Has accused the testator of a crime for which the law prescribed imprisonment for 6 years or more, if the accusation has been found groundless;
3. Has been convicted of adultery or concubinage with the spouse of the testator;
4. Has caused the testator to make a will or change one already made, by fraud, violence, intimidation, or undue influence;
5. A refusal without justifiable cause to support the parent or ascendant who disinherits such child or descendant;
6. Maltreatment of the testator by word or deed, by the child or descendant;
7. When a child or descendant leads a dishonorable or disgraceful life;
8. Conviction of a crime which carries with it the penalty of civil interdiction.

**Causes for the disinheritance of parents and ascendants, legitimate as well as illegitimate:**

1. When the parents have abandoned their children or induced their daughters to live a corrupt or immoral life, or attempted against their virtue;
2. When the parent or ascendant has been convicted of an attempt against the life of the testator, his or her spouse, descendants, or ascendants;
3. When the parent or ascendant has accused the testator of a crime for which the law prescribes imprisonment for six years or more, if the accusation has been found to be false;
4. When the parent or ascendant has been convicted of adultery or concubinage with the spouse of the testator;
5. When the parent or ascendant by fraud, violence, intimidation, or undue influence causes the testator to make a will or to change one already made;

6. The loss of parental authority for causes specified in this Code;
  - a. Judicial deprivation of parental authority in the ground of sexual abuse;
  - b. As a result of judicial declaration of abandonment of a child;
  - c. Harsh or cruel treatment, corrupting orders, compelling the child to beg, subjecting the child or allowing him to be subjected to acts of lasciviousness.
7. The refusal to support the children or descendants without justifiable cause;
8. An attempt by one of the parents against the life of the other, unless there has been a reconciliation between them.

**Causes for the disinheritance of a spouse:**

1. When the spouse has been convicted of an attempt against the life of the testator, his or her descendants, or ascendants;
2. When the spouse has accused the testator of a crime for which the law prescribes imprisonment of six years or more, and the accusation has been found to be false;
3. When the spouse by fraud, violence, intimidation, or undue influence cause the testator to make a will or to change one already made;
4. When the spouse has given cause for legal separation;
5. When the spouse has given grounds for the loss of parental authority;
6. Unjustifiable refusal to support the children or the other spouse.

**Legal or Intestate Succession**

**Order of Intestate Succession**

1. Legitimate Children/descendants;
2. Illegitimate Children/descendants;
3. Legitimate Parents/ascendants;
4. Illegitimate Parents;
5. Surviving Spouse;
6. Brothers, Sisters, Nephews and Nieces;
7. Other Collateral Relatives - to the 5th degree;
8. State

**Collateral Relatives**

Consanguinity - is the relation of persons descending from the same stock or common ancestors.

Lineal consanguinity - may be descending or ascending, is that which subsists between persons of whom one is descended in a direct line from the other.

Collateral consanguinity - is that which subsists between persons who have the same ancestors, but who do not descend or ascend one from the other.

**Right of Representation** - created by fiction of law, by virtue of which the representative is raised to the place and the degree of the person represented, and acquires the rights which the latter would have if he were living or if he could have inherited. (Art. 970)

The representative is called to succession by the law and not by the person represented. The representative does not succeed the person represented but the one whom the person represented would have succeeded.

This right takes place in the direct descending line, but never in the ascending. In the collateral line, it takes place only in favor of the children of brothers or sisters, whether they be of the full or half blood.

There is no representation in testamentary succession.

Applicable in cases of:

1. Predecease;
2. Incapacity or Unworthiness;
3. Disinheritance

**ADOPTED:** representation of and by an adopted child is not allowed. Stated otherwise, an adopted can neither represent nor be represented.

**RATIONALE:** the legal relationship created by adoption is strictly between the adopter and the adopted. It does not extend to the relatives of either party.

**Illegitimate Child has no right to inherit under intestate succession from:**

1. Legitimate children of his father or mother; and
2. Relatives of his father or mother and vice versa

## Chapter 2. Estate Tax

### Definition and Nature

**Estate Tax** - imposed on the transfer of property from the decedent to the heirs. It is an excise tax on the privilege to transfer property at the time of death.

### Justification for the Imposition of Estate Tax

1. Benefit-received theory - the law considers the service rendered by the government in the distribution of the estate of the decedent, either by law or in accordance with his wishes. For the performance of this services and other benefits that accrue to the estate and the heirs, the State collects the tax.
2. Privilege or State Partnership theory - inheritance is not a right but a privilege granted by the State and legatees have been acquired only with the protection of the State.
3. Ability to pay theory - receipt of inheritance which is in the nature of an unearned wealth or windfall, are placed assets into the hands of the heirs and beneficiaries. This creates an ability to pay the tax and thus contributes to government income.
4. Redistribution of wealth theory - receipt of inheritance is a contributing factor to the inequalities in wealth and income. The imposition of estate tax reduces the property received by the successor, thus helping to promote equitable distribution of wealth in society.

### Gross Estate

#### Kinds of Decedent for Estate Tax Purposes

1. Resident and citizens - taxed on all real or personal, tangible or intangible, wherever situated.
2. Non-resident alien - is taxable only for his properties within the Philippines, subject to the reciprocity clause.

**Reciprocity clause** - no tax shall be collected in respect of intangible personal property:

- a. if the decedent at the time of his death or the donor at the time of his donation was a citizen and resident of a foreign country which at the time of his death or donation did not impose a transfer tax of any character, in respect of intangible personal property of citizens of the Philippines not residing in that foreign country, or
- b. if the laws of the foreign country in which the decedent or donor was a citizen and resident at the time of his death or donation allows a similar exemption from transfer or death taxes of every character in respect of intangible personal property owned by citizens of the Philippines not residing in that foreign country.

#### Valuation

In general, the value of the properties shall be determined as the fair market value at the time of the decedent's death.

1. Real property - whichever is higher of the following:
  - a. FMV as determined by the Commissioner of Internal Revenue

- b. FMV as shown in the schedule of values fixed by the provincial or city assessors.
2. Personal Property and Shares of Stock - depending whether:
    - a. Personal property - FMV at the time of death
    - b. Unlisted common share - book value per share
    - c. Unlisted preferred shares - par value per share
    - d. Listed or traded in stock exchange - FMV shall be the arithmetic mean between the highest and lowest quotation at the date nearest the date of death, if none is available on the date itself.
  3. Right of usufruct, use or habitation, and annuity - there shall be taken into account the probable life of the beneficiary in accordance with the latest basic standard mortality table, to be approved by the Secretary of Finance, upon recommendation of the Insurance Commissioner.

#### Inclusions in the Gross Estate

1. Properties owned by the decedent actually and physically present in the estate:
  - a. **Real properties and tangible personal properties** - the residency of the deceased as well as the location of the properties would be determinative of inclusion in the gross estate.
  - b. **Intangible personal properties** - the following are considered to be intangible personal properties located within the Philippines:
    - i. Franchise which must be exercised in the Philippines;
    - ii. Shares, obligations, or bonds issued by any corporation or sociedad anonima organized or constructed in the Philippines in accordance with its laws;
    - iii. Shares, obligations, or bonds issued by any foreign corporation, 85% of the business of which is located in the Philippines;
    - iv. Shares, obligations, or bonds issued by any foreign corporation, if such shares, obligations or bonds have acquired business situs in the Philippines; and
    - v. Shares or rights in any partnership, business, or industry.
2. **Decedent's interest** - refers to the extent of equity or ownership participation of the decedent on any property physically existing and present in the gross estate, whether or not in his possession, control or dominion. Included up to the extent of the interest therein at the time of his death. (e.g. share in joint account or dividends declared prior to decedent's death)
3. Property not physically in the estate:
  - a. **Transfer in contemplation of death** - the thought of death serves as a controlling motive which induces the disposition of the property for the purpose of avoiding estate tax. It has two types:
    - i. Transfer of property intended to take effect after death;
    - ii. Transfer to take effect after death where the decedent retained the possession or

enjoyment of, or right to the income from property; or the right to designate the person who shall possess or enjoy the property of the income therefrom.

In the second type, the inheritance may have been delivered or transferred already but the right to fruit has been reserved.

EXCEPTION: if the transfer was made under a bona fide sale for an adequate consideration and full consideration of money or money's worth.

b. **Transfer with retention or reservation of certain rights** - same with a.ii. but the thought of death as a controlling motive to dispose properties is absent.

c. **Revocable transfers** - is one where the terms of enjoyment of the property may be altered, amended, revoked or terminated by the decedent. It is sufficient that the decedent has the power to revoke, though he did not exercise the power to revoke.

d. **Transfer under a general power of appointment** - included in the gross estate to the extent of any property passing under a general power of appointment exercised by the decedent.

- i. General Power of Appointment - is one which may be exercised in favor of anybody, including the decedent.
- ii. Special Power of Appointment - is one which may be exercised only in favor of a certain person or persons designated by the prior decedent.

May be exercised by the donor-decedent by will, by deed to take effect at or after his death, or by deed under which he has retained for his life (a) the possession or right to the income from the property or (b) the right to designate the persons who shall enjoy or possess the property or the income therefrom.

e. **Proceeds of Life Insurance** - proceeds of life insurance taken out by the decedent upon his life shall constitute part of the gross estate if the beneficiary is:

- i. The estate of the decedent, his executor or administrator;
- ii. A third person and the designation of the beneficiary is revocable.

Under the insurance code, a designation is revocable, unless stated expressly by the insured, and indicated in the policy, that the designation is irrevocable.

f. **Claims against insolvent person** - under Sec. 86 of the NIRC, claims against insolvent persons which are not collectible may be considered as deductions from the gross estate. For this to apply,

the whole amount of the claim must be included in the gross estate, regardless of collectability, and the amount uncollectible will be considered as a deduction. A judicial declaration of insolvency is not required but the incapacity of the debtor to pay his obligation should be proven.

g. **Transfers for Insufficient Consideration** - if the transfer is made for less than the market value of the property, the excess of the fair market value of the property at the time of death over the amount of consideration received is included in the gross estate.

- i. Fair market value at the time of sale or transfer - used to determine whether or not the consideration was full and adequate.
- ii. FMV of the property at the time of death - used to determine the amount to be included in the gross estate if the consideration received is substantially lower or for less than full and adequate consideration compared to the FMV at the time of sale or transfer. (Excess of FMV at the time of death over the consideration received)
- iii. If no consideration was received at the date of transfer and such transfer was made in contemplation of death - the FMV at the time of death should be included in the estate.
- iv. If no consideration was received at the date of transfer and such transfer was not made in contemplation of death - subject to Donor's tax based on the FMV at the time of transfer.

### Exclusions in the Gross Estate

A. Exclusions under Sections 85 and 86 of the Tax Code

1. **Exclusive property of the Surviving Spouse** - these properties are not owned by the decedent upon his death. Whether such property is exclusive or common will depend on the type of property relations of the husband and wife.

- a. Capital - exclusive properties of the husband
- b. Paraphernal - exclusive properties of the wife

2. **Properties outside the Philippines of a non-resident alien decedent.**

3. **Intangible personal property in the Philippines of a non-resident alien under the reciprocity law.**

B. Exclusions under Section 87 of the Tax Code

1. **Merger of usufruct in the owner of the naked title** - in this case, the usufruct and the naked title to the property were given to different persons. Upon the death of the usufructuary, the usufruct merges with the naked title. This merger is no longer subject to the estate tax since it has already been subjected thereto upon the death of the original owner thereof.

2. **The transmission or delivery of the inheritance or legacy by the fiduciary heir to the legatee to the fideicommissary** - elements of fideicommissary are:

- a. There is a first heir who is tasked to preserve the property and transmit it to the second heir.

- b. There is a second heir to whom the property will be transferred once the right of the first heir expires;
  - c. The second heir is one degree from the first heir - which can mean by relationship or by degree of transfer.
3. **The transmission or delivery from the first heir, legatee or donee in favor of another beneficiary, in accordance with the desire of the predecessor** - also known as "special power" of appointment
  4. **All bequests, devises, legacies or transfers to social welfare, cultural and charitable institutions**, no part of the net income of which insures to the benefit of any individual: Provided, however, That not more than thirty percent (30%) of the said bequests, devises, legacies or transfers shall be used by such institutions for administration purposes - does not include religious institutions. Accordingly, it is subject to estate tax. Note that the estate tax is an excise tax and not a property tax. As such, it is not covered by the exemption under Sec. 28(3), Art. VI of the 1987 Constitution, since such exemption covers only property taxes.

#### C. Exclusions under Special Laws

1. Proceeds of life insurance and benefits received by members of the GSIS (RA728)
2. Benefits received by members from the SSS by reason of death (RA172)
3. Amounts received from Philippine and United States governments for war damages.
4. Amounts received from United States Veterans Administration.
5. Benefits received from Philippine and US government for damages suffered during World War II (RA227)
6. Death benefits provided by an employer to its employees under RA4917.
7. Payments from the Philippines and US government to the legal heirs of deceased of World War II Veterans and deceased civilian for supplies/services furnished to the US and Philippine Army (RA136)
8. Life insurance proceeds on life insurance policy taken out by the decedent himself, upon his own life, where the beneficiary is a third person and is irrevocable designated.
9. Life insurance proceeds in Insurance Policy taken out by his employer on the employee's life, whoever the beneficiary maybe, whether the designation is revocable or irrevocable.

## Chapter 3. Deductions from the Gross Estate

### A. Ordinary Deductions

#### 1. Expenses, Losses, Indebtedness, Taxes, Etc. (ELITE)

**a. Funeral Expenses** - for actual funeral expenses or in an amount equal to five percent (5%) of the gross estate, whichever is lower, but in no case to exceed P200,000. This includes:

- a) mourning apparel of the surviving spouse and unmarried minor children of the deceased bought and used for the occasion of the burial;
- b) expenses during the decedent's wake, including food and drinks;
- c) publication charges of death notices;
- d) telecommunication expense incurred in informing relatives of the deceased;
- e) cost of burial plot, tombstone, monument or mausoleum, but not their upkeep;
- f) interment and/or cremation fees and charges; and
- g) all other expenses incurred in the performance of the rites and ceremonies incident to the interment.

Any amount in excess of the P200,000 shall not be allowed as a deduction, neither can the unpaid amount in excess of the P200,000 can be claimed as a deduction under "claims against the estate. (Sec. 6[A][1], RR No. 2-03) Supporting receipts or invoices or other evidence shall be furnished.

Note that the amount deductible must be advanced by the estate of the deceased to be to be deductible. Accordingly, if the expenses are paid for by the relatives or friends, then such will not be considered deductible.

**b. Judicial Expenses** - refers to expenses of testamentary or intestate proceedings which may include fees of the executor pr administrator, attorney's fees, court fees, accountant's fees, appraiser's fees, cost of preserving and distributing the estate, cost of storing and maintaining the property of the estate, and brokerage fees for selling the property "during the settlement period".

Settlement period - means not beyond the last day prescribed by law to file and pay the estate tax which is six (6) months from death or the extension (to file) thereof which is not more than 30 days after the lapse of the six month period.

Judicial expenses for estates under "extrajudicial proceedings" - allowed as deduction as long as the expenses incurred are essential to the administration and settlement of the estate (CIR vs Pajonar).

Note that attorney's fees paid by the heirs to their respective lawyers arising from conflicting claims are not deductible as judicial expenses. These expenses should

be separately borne by them.

There is no limit as to amount which may be claimed for judicial expenses.

**c. Indebtedness or Claims against the Estate** - refer to obligations contracted by the deceased, which is still enforceable after his death, for which his estate is now liable for. Requisites are:

- a) The liability represents a personal obligation of the deceased existing at the time of his death except unpaid funeral expenses and unpaid medical expenses;
- b) The liability was contracted in good faith and for adequate and full consideration in money or money's worth;
- c) The claim must be a debt or claim which is valid in law and enforceable in court;
- d) The indebtedness must not have been condoned by the creditor or the action to collect from the decedent must not have been prescribed. (Sec. 6[A][3][i], RR No. 2-03)

Substantiation requirements under (Sec. 6[A][3][ii], RR No. 2-03)

Simple loan (including advances):

- a) Debt instrument duly notarized at the time the indebtedness was incurred except for loans granted by financial institutions where notarization is not part of the business practice/policy of the financial institution lender;
- b) Notarized certification from the creditor as to the unpaid balance including interest upto the time of death;
- c) Proof of financial capacity of the creditor to the lend the amount at the time the loan was granted, as well as its latest audited balance sheet with a detailed schedule of its receivable showing the unpaid balance of the decedent-debtor;
- d) A statement under oath of the administrator or executor reflecting the disposition of the loan proceeds if said loan was contracted within 3 years from the decedent's death.

Unpaid obligation from purchase of goods or services:

- a) Pertinent documents evidencing the purchase of goods or service (e.g. sales invoice/delivery receipt, contract for the services agreed to be rendered, statement of account);
- b) Notarized certification from the creditor as to the unpaid balance including interest upto the time of death;
- c) Certified true copy of the latest audited balance sheet of the creditor with a detailed schedule of its receivable showing the unpaid balance of the decedent-debtor.

Where settlement is made through the Court in testate or intestate proceeding, pertinent documents filed with the Court evidencing the claims against the estate, the Court Order approving the said claims, if already issued, shall

be submitted in addition to the documents mentioned in the preceding paragraphs.

**d. Claims against insolvent persons** - since the debtor's properties are not sufficient to pay for all its obligations, the claims of his creditors will be satisfied out of the available properties only and thus may not be fully paid.

The amount that cannot be collected by the estate of the deceased will be the amount deductible for estate tax purposes. Provided, that the full amount of the claim is first included in the gross estate.

**e. Unpaid mortgage or indebtedness on property** - similar to claims against insolvent persons, the full value of the property to which the mortgage or indebtedness attaches to, must be included first in the gross estate before any deduction for such mortgage or indebtedness can be made.

If a loan is merely an accommodation loan, where the proceeds of such went to another person, the mortgage, to be deductible, the loan must first be included as a receivable of the estate.

**f. Taxes** - that accrue prior to the death of the decedent, but remain unpaid, are also deductible for estate tax purposes.

Under Sec. 86(A)(1)(e) of the NIRC, the following taxes are not deductible:

- a) Income tax on income received after death;
- b) Property taxes not accrued before death; and
- c) Estate tax.

**g. Losses** - are deductible when all of the following conditions are satisfied:

- a) The loss arose from fire, storm, shipwreck, or other casualty, robbery, theft or embezzlement;
- b) Not compensated by insurance or otherwise;
- c) Not claimed as deduction in an income tax return of the estate subject to income tax;
- d) Occurring during the settlement of the estate and before the last day for the payment of the estate tax or within 6 months from the date of death of the decedent.

However, the property subject to the loss, must be included in the gross estate for the item to be deductible.

**2. Vanishing Deductions** - also referred to as a deduction for "property previously taxed". Since transfer tax is imposed on each transfer, a vanishing deduction is allowed to ease the burden of heavy taxes on properties that switch hands within a short period of time.

Requisites:

- a) The current decedent died within 5 years from receipt of the property from the prior decedent/donor;
- b) The property on which the vanishing deduction is being claimed is located in the Philippines;
- c) The property must have formed part of the taxable estate of the prior decedent or of the taxable gift of the donor;
- d) The estate tax/donor's tax must have been finally determined and paid;
- e) The property on which vanishing deduction is being claimed must be identified as the one received from the prior decedent, or from donor, or something acquired in exchange therefor;
- f) No vanishing deduction was allowable to the estate of the prior decedent.

Note: There is no need for there to be two succeeding deaths for the deduction to apply, since the deduction will also apply if the property was received as a gift from the previous owner and the donor's tax has already been paid therefor.

Reductions to the basis for computing the vanishing deduction:

- a) Mortgage or indebtedness on the property paid for by the current decedent;
- b) Ratio of the property (value to take net of mortgage paid) to the gross estate as to deductions claimed for estate tax (excluding standard deduction, family home, medical expenses, and amounts received under RA No. 4917)

Pro-forma computation of vanishing deduction:

Value to take	Pxxx
(Lower amount bet. the value of the property in the gross estate of the prior decedent or value of the gift and value of the same property in the gross estate if the present decedent)	
Less: Mortgage paid	(xxx)
(Paid by the present decedent from the mortgage assumed when the property was inherited or received as donation)	
<b>Initial Basis</b>	<b>xxx</b>
Less: Proportionate deduction	
$\frac{\text{Initial basis}}{\text{Gross Estate}} \times \text{ELITE} + \text{Transfer for public use}$	
	(xxx)
Final Basis	xxx
Multiply by: Vanishing Deduction %	%
<b>Vanishing Deduction</b>	<b>xxx</b>

**3. Transfer for Public Use** - the amount of all the bequests, legacies, devises or transfers to or for the use of the Government of the Republic of the Philippines, or any political subdivision thereof, for exclusively public purposes.

The property must first be included in the gross estate for this item to be deductible.

## B. Special Deductions

**1. Family Home** - amount deductible is equivalent to the current fair market value of the decedent's family home. Provided, however, that if the said current fair market value exceeds P1,000,000, the excess shall be subject to estate tax.

Definition of family home - the dwelling house, including the land on which it is situated, where the husband and wife, or a head of the family, and members of their family reside. The family home is deemed constituted on the house and lot from the time it is actually occupied as a family residence and is considered as such for as long as any of its beneficiaries actually resides therein. (Arts. 152 and 153, Family Code)

The actual occupancy of the house as the family residence shall not be considered interrupted or abandoned in such cases as the temporary absence from the constituted family home due to travel or studies or work abroad, etc.

In other words, the family home is generally characterized by permanency, that is, the place to which, whenever absent for business or pleasure, one still intends to return.

For purposes of availing of a family home deduction to the extent allowable, a person may constitute only one family home.

Conditions for deductibility:

- a) The family home must be the actual residential home of the decedent and his family at the time of death, as certified by the Barangay Captain of the locality where the family home is situated;
- b) The total value of the family home must be included as part of the gross estate of the decedent; and
- c) Allowable deduction must be equivalent to the current fair market value of the family home as declared or included in the gross estate, or the extent of the decedent's interest, whichever is lower, but not exceeding P1,000,000.

**2. Standard Deduction** - the amount deductible is equivalent to P1,000,000. This amount shall be allowed as an additional deduction without need of substantiation.

**3. Medical Expenses** - medical expenses incurred by the decedent within one (1) year prior to his death which is duly substantiated with receipts shall be allowed as deduction for estate tax purposes. Provided, that in no case shall the deductible medical expenses exceed P500,000.

Requisites:

- a) All medical expenses (cost of medicines, hospital bills, doctor's fees, etc.) incurred (whether paid or unpaid) within 1 year before the death of the decedent;
- b) The same are duly substantiated with official receipts for services rendered by the decedent's attending physicians, invoices, statements of account duly certified by the hospital, and such other documents in support thereof;
- c) That the amount thereof, whether paid or unpaid, does not exceed P500,000.

**4. Amount received under RA No. 4917** - any amount received by the heirs from the decedent - employee as a consequence of the death of the decedent employee in accordance with RA No. 4917 shall be allowed as deduction for estate tax purposes. Provided, that such amount is included in the gross estate of the decedent.

## C. Net Share of the Surviving Spouse

The amount deductible under this category is the net share of the surviving spouse in the conjugal partnership property. The net share is equivalent to 1/2 or 50% of the conjugal property after deducting the obligations chargeable to such property.

The effect is that, ordinary deductions are deducted from the column of the conjugal properties, effectively reducing the amount of net conjugal assets, half of which will be the deduction.

## D. Allowable Deductions for Nonresident Alien Decedent

The following are the allowable deductions from the gross estate of a non-resident aliens:

1. A ratable portion of ELITE, regardless of where it was incurred or paid, as follows:  
$$\frac{\text{Gross Estate - Philippines}}{\text{Gross Estate - World}} \times \text{World ELIT}$$
2. Transfer for public use;
3. Vanishing deductions;
4. Net share of the surviving spouse in the conjugal or community property.

No deduction shall be allowed in the case of a non-resident not a citizen of the Philippines, unless the executor, administrator, or anyone of the heirs, as the case may be, includes in the return required to be filed the value at the time of his death of that part of the gross estate not situated in the Philippines. (Sec. 86[D], NIRC)

## Chapter 5. Estate Tax Credit and Estate Tax Distributable

### A. Rates of Estate Tax

OVER	BUT NOT OVER	THE TAX SHALL BE	PLUS	OF EXCESS OVER
	P 200,000	Exempt		
P 200,000	500,000	0	5%	P 200,000
500,000	2,000,000	P 15,000	8%	500,000
2,000,000	5,000,000	135,000	11%	2,000,000
5,000,000	10,000,000	465,000	15%	5,000,000
10,000,000	And Over	1,215,000	20%	10,000,000

### B. Estate Tax Credit

In general - estate tax shall be credited with the amounts of estate tax imposed by the authority of a foreign country.

The net estate of a citizen of the Philippines and a resident alien includes his properties which are outside the Philippines which may have been subjected already to estate tax in the country where it is situated and is also subject to estate tax in the Philippines.

Limitations:

#### a. One foreign country

Limit 1 - Lower amount between the following:

$$\frac{\text{Net estate, foreign country}}{\text{Net estate, world}} \times \text{Phil. Estate Tax} = \text{Pxxx (Limit)}$$

#### Versus

$$\text{Actual Tax paid, foreign country} = \text{Pxxx (Actual)}$$

#### b. Two or more foreign countries

Step 1. Compute for Limit 1 per foreign country as shown above.

Step 2. Compute for Limit 2 by getting the lower amount between the following:

$$\frac{\text{Net estate, all foreign country}}{\text{Net estate, world}} \times \text{Phil. Estate Tax} = \text{Pxxx (Limit)}$$

#### Versus

$$\text{Actual Tax paid, all foreign countries} = \text{Pxxx (Actual)}$$

Step 3. Choose the lower amount between Limit A and Limit B.

Note: For countries with negative estate, no need to compute for Limit 1. But this shall be included in computing Limit 2.

### C. Net Distributable Estate

Net distributable estate is the amount arrived at from gross estate consisting all properties in the possession and control of the decedent at the time of death and actual expenses, charges, and payments from the gross estate.

Gross Estate	Distributable Estate
Real or immovable property	included
Tangible personal property	included
Intangible personal property	included
Transfers in contemplation of death	not included
Revocable transfers	not included
Transfers under the general power of appointment	not included
Proceeds of Life Insurance	included
Exclusions such as SSS, GSIS, etc.	included
<b>Allowable Deductions</b>	
Funeral expenses	actual
Judicial	actual
Unpaid taxes	actual
Claims against the estate	actual
Claims against insolvent person	actual
Losses	actual
Transfer for public use	actual
Vanishing deduction	not considered
Standard deduction	not considered
Family home	not considered
Medical expenses	actual
Amount received under RA 4917	not considered
Share of surviving spouse	as computed

**Less: Estate Tax Due**

xxx

**Net Distributable Estate**

xxx

### D. Administrative Provisions

**Notice of Death** - In all cases of transfers subject to tax, or where, though exempt from tax, the **gross value of the estate exceeds P20,000**, the executor, administrator or any legal heirs, as the case may be, **within 2 months after the decedent's death**, or

within a like period after qualifying as such executor or administrator, shall give a written notice thereof to the Commissioner.

### **Estate Tax Return (BIR Form No. 1801)**

An estate tax is required to be filed when:

1. The estate is subject to tax;
2. If exempt from tax, the gross estate exceeds P200,000;
3. Regardless of the amount of the gross estate, where said estate consists of registered property, motor vehicle, shares of stock, or other similar property for which clearance form the BIR is required as a condition precedent for the transfer of ownership.

The return shall contain the following:

1. Value of the gross estate of the decedent at the time of his death, or in case of a non-resident, not a citizen of the Philippines, that part of his gross estate situated in the Philippines;
2. The deductions allowed from gross estate;
3. Such information as may at the time be ascertainable and such supplemental data as may be necessary to establish the correct taxes. Provided, however, that the estate tax returns showing a gross value exceeding P2,000,000 shall be supported with a statement duly certified by a Certified Public Accountant containing the following:
  - a. Itemized assets of the decedent with their corresponding value at the time of death;
  - b. Itemized deductions from gross estate;
  - c. Amount of tax due whether paid or outstanding.

### **Place of Filing:**

1. In case of a resident decedent, the administrator or executor shall register the estate of the decedent and secure a new TIN from the RDO where the decedent was domiciled at the time of his death. The estate tax return and the tax due thereon shall be filed and paid with the Authorized Agent Bank (AAB), RDO, Collection Officer or duly authorized city or municipal treasurer where the decedent was domiciled at the time of death, whichever is applicable.
2. Non-resident citizen or alien, with executor or administrator in the Philippines, the estate tax return shall be filed and the TIN for the estate secured from the RDO where such executor or administrator is registered, or if not registered, the RDO having jurisdiction over his residence.
3. Non-resident citizen or alien, without an executor or administrator in the Philippines – the estate tax shall be filed and the TIN for the estate shall be secured from the Office of the Commissioner through RDO 39 – South Quezon City.

**Liability for payment** - The estate tax shall be paid by the executor or administrator before delivery to any beneficiary of his distributive share of the estate. Such beneficiary shall to the extent of his distributive share of the estate, be subsidiarily liable for the payment of such portion of the estate tax as his distributive share bears to the value of the total net estate.

**Accrual vs. Payment of Tax** - the estate tax accrues from the time of death; while payment of the estate tax is at the time the estate tax return is filed, which is 6 months from the decedent's death.

Extension for payment of tax - in meritorious cases, an extension not exceeding 30 days may be granted by the Commissioner or any other Revenue Office authorized by him, for the filing of the return.

For the payment of tax - an extension not to exceed 5 years in case of judicial settlements, or 2 years in extrajudicial settlements, may be granted if the Commissioner finds that the payment of estate tax or any part thereof would impose undue hardship upon the estate or any heirs. The running of the statute of limitations for deficiency assessment shall be suspended for the period of such extension. (Sec. 9 of RR No. 2-2003)

**Effect - Extension of time to File and Pay the Estate Tax** - the Commissioner or his duly authorized representative may require the executor, or administrator, or beneficiary, to furnish a bond in such amount, not exceeding double the amount of the tax and with such sureties as the Commissioner deems necessary, conditioned upon the payment of the said tax in accordance with the terms of the extension.

**Payment on Installment** - In case the available cash of the estate is not sufficient to pay its total estate tax liability, the estate may be allowed to pay the tax by installment and a clearance shall be released only with respect to the property the corresponding/computed tax on which has been paid. There shall, therefore, be as many clearances (Certificates Authorizing Registration) as there are as many properties released because they have been paid for by the installment payments of the estate tax. The computation of the estate tax, however, shall always be on the cumulative amount of the net taxable estate. Any amount paid after the statutory due date of the tax shall be imposed the corresponding applicable penalty thereto. However, if the payment of the tax after the due date is approved by the Commissioner or his duly authorized representative, the imposable penalty thereon shall only be the interest.

**Surcharges and Interest** - any amount paid after the statutory period to pay the tax, but within the extension period shall not be subject to surcharge. However, the 20% interest continues to run until actual date of payment.