REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

CALTEX (PHILIPPINES) INC.,
Petitioner,

- versus -

C.T.A. CASE NO. 4986

THE COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:
OCT 06 1995

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DECISION

This is a judicial claim for the issuance of a tax credit certificate in the amount of P1,972,789.00 representing alleged excess tax withheld on cash dividends paid to a stockholder in the year 1991.

Petitioner is a domestic corporation, organized and existing under the laws of the Philippines and among its shareholders are two corporate entities namely: Caltex Petroleum Corporation (CPC) organized under the laws of the United States and Caltex Investment and Trading Limited (CITL), a foreign corporation organized under the laws of Bermuda. The latter corporation subsequently changed its corporate name to Traders Insurance Limited

(TIL) as evidenced by a certificate of incorporation on Change of Name (Exhibit "D"), dated March 31, 1993.

On April 30, 1991, the Board of Directors of petitioner declared cash dividends in the amount of P145,000,000.00 as part of its December 31, 1990 retained earnings (see Exhibit "G") and as a consequence cash dividends were paid to their stockholders of record in proportion to the respective shares of stock owned by them. It is alleged in the petition that CPC earned a total amount of P105,544,216.00 as cash dividends while CITL earned P39,455,784.00 pursuant to the above-mentioned declaration. It is further alleged that the petitioner, as withholding agent and in accordance with the withholding tax regulations, deducted a 20% tax rate on the cash dividends paid to these two stockholders, computed as follows:

	Amount of Dividend	20% tax rate applied
CPC	P105,544,216.00	P21,108,813.00
CITL	39,455,784.00	7,891,157.00
	TOTAL TAX WITHHELD	P29,000,000.00

As withholding agent, petitioner allegedly paid the total amount of P29,000,000.00 to the BIR, through its agent Citytrust Bank, and presented as evidence the BIR Confirmation Receipt in the said amount (Exhibit "A"). It also presented its monthly remittance return filed on

P29,000,000.00 corresponding to the taxes it withheld from dividend payments made in April of 1991.

Working on the theory that the tax rate applicable is 15% instead of the 20% tax imposed, petitioner filed a letter requesting for a tax credit certificate in the amount of P1,972,789.00 which represents the difference between the 20% tax withheld and the 15% tax rate computed as follows:

I.	P39,455,784	-	Dividends due CITL
	x 20%	-	Tax Withheld by CPI
	P 7,891,157	-	Tax remitted and paid to BIR
II.	P39,455,784	-	Dividends due CITL
	x 15%	-	Tax rate under Sec. 25, Tax Code
	P 5,918,367.60	-	Tax that should have been remitted to BIR
III.	P 7,891,157	-	Tax remitted to BIR
	- P 5,918,367.60	-	Correct Amount of Tax
	₱ 1,972,789.40	-	Amount for refund

Petitioner's letter, received by the BIR on March 26, 1992, cited the case of **Procter and Gamble Philippines vs. Commissioner of Internal Revenue**, 204 SCRA 377, where the Supreme Court upheld the right of Procter and Gamble Philippines to a 15% tax rate on the dividends it remitted to its non-resident corporate stockholder. This claim for tax credit was left unanswered by respondent so petitioner sought relief from this Court through a petition for review filed on May 7, 1993 reiterating therein the same grounds found in his letter to the BIR.

Respondent proposed the following Special and Affirmative Defenses:

5. Petitioner's claim for refund is still under administrative investigation;

6. Petitioner is not entitled to the refund sought under the provisions of Section 25(b)(5)(B) of the National Internal Revenue Code since it is not shown with certainty that it is entitled thereto such that the country in which the non-resident foreign corporation is domiciled has allowed a credit against the tax due from the non-resident foreign corporation. Well-settled is the rule that provisions on tax refund are construed strictly against the taxpayer as they are in the nature of tax exemption;

7. In an action for refund, the taxpayer has the burden to show that the taxes paid were erroneously or illegally paid and failure to sustain said burden is fatal to the action for refund;

8. It is incumbent upon petitioner to show that it has complied with the provisions of Section 204(3) and 230 of the Tax Code, as amended. Petitioner has to show that it has paid the full amount of the tax a partial amount of which it seeks for refund.

The sole issue in this case is whether or not petitioner corporation is entitled to the preferential rate of 15% withholding tax on dividends remitted to CITL presently named TIL, its corporate stockholder domiciled in Bermuda. However basic to the determination of this issue is the resolution of the question of whether or not Bermuda, the country where the stockholder is based, allows as tax credit the 20% Philippine tax on such dividends.

Petitioner maintains in its petition that the claim for refund or tax credit is premised on the provision of law found in Section 25(b)(5)(B) of the National Internal Revenue Code which provides, thus:

> (5) Tax on certain incomes received by non-resident foreign corporations -
>
> (B) On dividends received from a domestic corporation liable to tax under this chapter, the tax shall be 15% of the dividends received, which shall be collected and paid as provided in Section 51(a) of the National Internal Revenue Code, as amended, subject to the condition that the country in which the non-resident foreign corporation is domiciled shall allow a credit against the tax due from the non-resident foreign corporation; taxes deemed to have been paid in the Philippines equivalent to 20% which represents the difference between the regular tax (35%) on corporations and the tax (15%) on dividends as provided in this subparagraph.

To support its claim, petitioner tried to show this Court that the aforecited provision of the law applies squarely to the present situation. When cash dividends were declared by petitioner in April 1991, CITL earned a total amount of P39,455,784.00 out of which P7,891,157.00

representing the 20% withholding tax at source was deducted. Petitioner further claims that CITL as a non-resident foreign corporation is entitled to only a 15% tax rate on the dividends it received because the Commonwealth of Bermuda, the country where CITL has its domicile, virtually exempts dividends received for its overseas investment from taxes, thus there is already sufficient compliance with the condition provided by Section 25(b)(5)(B) of the Tax Code. To prove that Bermuda exempts dividend payments from taxes, petitioner presented as evidence an authenticated copy of a Certificate of Assurance issued by the Minister of Finance of Bermuda (Exhibit "K") which provides in part:

> xxxx in the event of there being enacted in these Islands any legislation imposing tax computed on profits or income, or computed in any capital asset, gain or appreciation, or any tax in the nature of estate duty or inheritance tax, then the imposition of any such tax shall not be applicable to
>
> CALTEX INVESTMENTS AND TRADING LIMITED
>
> xxxxxxxxxxx

Moreover, petitioner presented a copy of the BIR ruling, dated March 18, 1988 (Exhibit "I"), where the then Commissioner Bienvenido A. Tan declared that a non-resident corporation domiciled in Bermuda is subject only to the 15% withholding tax prescribed by Section 25(b)(5)(B) of the Tax Code, "it having been established that Bermuda does not impose any tax on dividends that Bermuda does not impose any tax on dividends received by the corporation domiciled therein; (The Exempted Undertakings Tax Protection Act 1966)".

Apart from those already mentioned, petitioner formally offered the following exhibits:

"E"	Journal entry of Caltex Investments & Trading, Ltd.	To prove that 14,579,440 shares were issued to Caltex Investments & Trading, Ltd.
"E-1"	Journal Entry of Traders Insurance Ltd.	To prove the share-holdings of Traders Insurance, Ltd.
"E-2"	Ledger entry on Caltex Investments & Trading, Ltd.	To prove that 14,579,440 shares issued in the name of Caltex Investments & Trading, Ltd. were subsequently cancelled.
"F"	Stock Certificate No. 111 of Caltex (Phils.), Inc. for 14,579,440 issued in the name of Caltex Investments & Trading, Ltd.	To prove the share-holding of Caltex Investments & Trading, Ltd. in Caltex (Phils.), Inc.
"F-1"	Stock Certificate No. 136 of Caltex (Phils.), Inc. issued in the name of Traders Insurance Ltd. for 14,579,440 shares.	To prove the share-holding of Traders Insurance Ltd. as a result of the transfer of shares by Caltex Investments & Trading, Ltd.

Respondent did not offer any evidence and opted not to submit her Memorandum.

Section 25(b)(5)(B) of the Tax Code which is at the center of this controversy has already triggered an abundance of jurisprudence, the most recent of which is the Resolution promulgated by the Supreme Court in the case entitled **Commissioner of Internal Revenue vs. Procter and Gamble Philippine Manufacturing Corporation**, 204 SCRA 377 dated December 2, 1991. This resolution in effect reversed the High Court's earlier decision when it upheld the right of Procter and Gamble Philippines to a preferential tax rate of 15% on the dividends it remitted to its parent corporation domiciled in the USA. The Supreme Court declared that the 15% tax rate shall be applied if the country of domicile of the non-resident corporate stockholder allows such foreign corporation a tax credit "for taxes deemed paid in the Philippines", thus:

> "The ordinary 35% tax rate applicable to dividend remittances to non-resident corporate stockholders of a Philippine corporation, goes down to 15% if the country of domicile of the foreign stockholder corporation "shall allow" such foreign corporation a tax credit for "taxes deemed paid in the Philippines," applicable against the tax payable to the domiciliary country by the foreign stockholder corporation. In other words, in the instant case, the reduced fifteen percent (15%) dividend tax rate is applicable if the USA "shall allow" to P and G USA a tax credit for

> "taxes deemed paid in the Philippines" applicable against the US taxes of P and G USA.
>
> The NIRC specifies that such tax credit for "taxes deemed paid in the Philippines" must, as a minimum, reach an amount equivalent to 20 percentage points which represents the difference between the regular 35% dividend tax rate and the preferred 15% dividend tax rate."

This ruling is in consonance with the spirit and intention of P.D. 369 which introduced the aforecited provision of the law to the National Internal Revenue Code, as enunciated by the Procter and Gamble case, thus:

> "The economic objectives sought to be achieved by the Philippine Government by reducing the 35% dividend rate to 15% are set out in the preambular clauses of P.D. No. 369 which amended Section 24 (b)(1) NIRC, into its present form:
>
> > WHEREAS, it is imperative to adopt measures responsive to the requirements of a developing economy foremost of which is the financing of economic development programs;
> >
> > WHEREAS, non-resident foreign corporations with investments in the Philippines are taxed on their earnings from dividends at the rate of 35%;
> >
> > WHEREAS, in order to encourage more capital investment for large profits an appropriate tax need be imposed on dividends received by non-resident foreign corporations in the same manner as the tax imposed on interest on foreign loans;"

To be able to implement the intention of the above-mentioned law, the Supreme Court interpreted Section 25(b)(5)(B) with liberality when it ruled:

> "It is important to note that Section 24 (b)(1), NIRC, does not require that the US must give a "deemed paid" tax credit for the dividend tax (20 percentage points) waived by the Philippines in making applicable the preferred dividend tax rate of 15%. In other words, our NIRC does not require that the US tax law deem the parent - corporation to have paid the 20 percentage points of dividend tax waived by the Philippines. <u>The NIRC only requires that the US "shall allow" P and G USA a "deemed paid" tax credit in an amount equivalent to the 20 percentage points waived by the Philippines.</u> (Underscoring supplied)

Reciprocity is the key element in the application of the 15% preferential tax rate. The country of domicile of the non-resident corporate stockholder must grant the investor corporation a "deemed paid" tax credit at least equal in amount to the 20 percentage points of dividend tax foregone by the Philippines. In the words of Justice Paras found in his Dissenting Opinion:

> "It is evident that without reciprocity the desired consequences of the tax credit under P.D. 369 would be rendered unattainable."

In the instant case, the petitioner contends that Bermuda exempts dividends earned by CITL now (TIL) from taxes, therefore, there is sufficient compliance with the provision found in Section 25(b)(5)(B) of the Tax Code because this set-up "virtually prevented the imposition of double taxation, which is the very rationale behind the tax sparing provision of Section 25(b)(5)(B) of the Tax Code". (see p. 101, CTA Records). Respondent on the other hand challenges the claim of petitioner on the ground that it has not sufficiently established that the country in which the non-resident foreign corporation is domiciled has "allowed a tax credit against the tax due from the non-resident foreign corporation".

Based on the records of this case, we believe that petitioner has sufficiently proved the validity of its claim for a tax credit certificate. Petitioner remitted cash dividends to its foreign corporate stockholders in April of 1991 out of which a 20% tax were imposed and withheld as shown by the BIR Confirmation Receipt (Exhibit "A") and its Monthly Remittance Return for the aforementioned month (Exhibit "C"). A refund is now being claimed by petitioner on the portion of the taxes it withheld from the dividends it remitted to CITL now TIL), a corporation domiciled in Bermuda on the ground that the taxes should have been 15% instead of 20%. Evidence submitted by petitioner as well as previous BIR Ruling 111 dated March 18, 1988 show that Bermuda, the country of domicile of TIL exempts profits derived by its corporations from its overseas investments from taxes, therefore, the purpose of the tax provision imposing a 15% instead of a 35% tax rate has been fulfilled. The aforecited BIR Ruling No. 111 dated March 18, 1988 is significant, and we deem it necessary to quote portions of the said ruling, to wit:

RULING No. 111
March 18, 1988

25(b) (5)(B)	195-81	111-88

Gentlemen:

In reply to your letter dated November 20, 1987, I have the honor to inform you that it having been established that Bermuda does not impose any tax on dividends received by corporations domiciled therein, (The Exempted Undertakings Tax Protection Act 1966) the dividends to be remitted by TMX Philippines, Inc. to TMX Ltd. of Bermuda, a non-resident corporation domiciled in Bermuda are subject only to the 15% withholding tax prescribed by Section 25(b)(5)(B) of the Tax Code, as amended.

Very Truly yours,

(Sgd.) BIENVENIDO A. TAN, JR.
Commissioner

In the case of **Commissioner of Internal Revenue vs. Wander Philippines, Inc.**, 160 SCRA 573, the Supreme Court considered a total exemption from taxes by the country of domicile of the non-resident corporate stockholder on the dividends received, as sufficient basis for the applicability of the 15% tax rate, thus:

"While it may be true that claims for refund are construed strictly against the claimant, nevertheless, the fact that Switzerland did not impose any tax on the dividends received by Glaro from the Philippines should be considered as a full satisfaction of the given condition. For, as aptly stated by respondent court, to deny private respondent the privilege to withhold only 15% tax provided for under Presidential Decree No. 369 amending Section 24 (b)(1) of the Tax Code, would run counter to the very spirit and intent of said law and definitely will adversely affect foreign corporation's interest here and discourage them from investing capital in our country."

IN VIEW OF THE FOREGOING, this Court grants petitioner's claim for a tax credit certificate. Respondent is hereby ordered to issue a tax credit certificate in petitioner's favor, in the total amount of P1,972,789.00 representing excess taxes withheld on dividend payments to CITL, now named TIL, for the month of April 1991.

SO ORDERED.

RAMON O. DE VEYRA
Associate Judge

WE CONCUR:

ERNESTO D. ACOSTA
Presiding Judge

MANUEL K. GRUBA
Associate Judge

CERTIFICATION

I hereby certify that the decision was reached after due consultation among the members of the Court of Tax Appeals in accordance with Section 13, Article VIII of the Constitution.

ERNESTO D. ACOSTA
Presiding Judge
Court of Tax Appeals