REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

ALLIED THREAD CO. INC.,
Petitioner,

- versus -

C.T.A. CASE NO. 5444

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:
OCT 12 1998

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DECISION

This case involves a claim for refund in the amount of P5,832,132.10 allegedly representing excess or overpaid final taxes on royalty payments covering the period from October 1994 to September 1996.

Petitioner is a domestic corporation duly organized and existing under the laws of the Philippines; and is registered with the Board of Investments as a preferred non-pioneer enterprise under PD No. 1789 for the rehabilitation of integrated threadmill per Certificate of Registration No. 83-496 (Exhibit B).

The records show that petitioner and English Sewing Ltd., a non-resident foreign corporation organized under the laws of United Kingdom, entered into a royalty agreement concerning the manufacture of thread and textile substance, whereby the former agreed to pay a royalty fee of 5% of net domestic and export sales in consideration for the transfer of know-how and technical assistance provided by the latter.(Exhs. A to A-12, pp. 123-135, CTA records)

For the period from October 1994 to September 1996, petitioner allegedly paid royalties to English Sewing Ltd. in the total amount of P58,321,286.00. Petitioner claims that out of this amount, it withheld and remitted to the BIR the total amount of P14,580,324.00 representing 25% final withholding taxes on its royalty payments for the said period.

On November 21, 1996, petitioner filed with the Bureau of Internal Revenue, an administrative claim for refund in the amount of P5,832,131.00 allegedly representing overpaid withholding tax at source for the period October 1994 to September 1996 (Exh. AA). Petitioner avers that it overpaid its withholding tax for the said period by erroneously applying the rate of 25% instead of the 15% tax rate pursuant to Article II(2)(a)(i) of the RP-UK Tax Treaty. It argues that it should have properly applied the 15% preferential rate afforded to BOI-registered enterprises engaged in preferred areas of activities. Details of the alleged overpaid amount of P5,832,131.10 are shown hereinbelow.

Gross Royalties	₱58,321,286.00
Withholding Tax at 25%	25%
Tax due at 25%	₱14,580,321.50
Tax actually paid	14,580,324.00
Less: Tax due at 15%	8,748,192.90
Overpaid withholding tax	5,832,131.10

As there was no respondent's action or decision on petitioner's request and the two year period prescribed for filing a petition for review was about to expire, petitioner filed the instant petition for review on November 27, 1996.

The issues presented before the Court for resolution are as follows:

1) whether or not the royalty payments remitted by a domestic corporation registered with the Board of Investments (as a preferred non-pioneer enterprise) to a non-resident foreign corporation based in the United Kingdom, is subject to a 15% withholding tax rate pursuant to the R.P.-U.K. Tax Treaty; and if in the affirmative;

2) whether or not petitioner has sufficiently established, by competent evidence, its entitlement to the amount of P5,832,131.10.

With respect to the first issue, it is appropriate to quote the pertinent provisions of the R.P.-U.K. Tax Treaty particularly article 11(2)(a)(i) and (b), thus:

> "(2) Such royalties may also be taxed in the Contracting State in which they arise, and

> according to the law of that state. However, the tax so charged shall not exceed:
>
> (a) 15 percent of the gross amount of the royalties where the royalties are paid:
>
> (i) by an enterprise registered with the Philippine Board of Investments and engaged in preferred areas of activity, or
>
> (b) in all other cases, 25 percent of the gross amount of the royalties. (Underscoring supplied)

It is clear from the above-quoted Tax Treaty that in the case of the Philippines, the tax that it can impose on royalties derived by a resident of United Kingdom from sources within the Philippines shall be at the rate of 15% in case of a Board of Investment-registered company engaged in preferred areas of activity. Based on the same Tax Treaty, supra, petitioner correctly enumerated the essential elements that must exist before the 15% preferential tax rates shall apply, to wit:

> a. The recipient of the royalty payments must be a resident of the United Kingdom,
>
> b. The payor of the royalties must be a resident of the Philippines, and
>
> c. The payor is a BOI-registered enterprise and engaged in preferred areas of activities.

To support its claim for refund, petitioner presented the Certificate of Registration issued by the Board of Investments to prove that it is registered as a preferred non-pioneer enterprise in accordance with the Omnibus Investment Code (Exhibit "B"). Petitioner also offered in evidence the various Monthly Remittance Returns of Income Taxes Withheld to prove the amount of royalty fees paid to English Sewing Limited and the corresponding 25% withholding taxes on said royalties paid to the BIR for the period covered by the claim. Significant also is the presentation of the Articles of Incorporation of English Sewing Limited to prove that the recipient of the royalty payments is a company registered under the laws of the United Kingdom (Exhibit "BB"). Furthermore, petitioner called this Court's attention to BIR Ruling No. DA-068-97, dated February 14, 1997, where it was declared that the royalty payments remitted by petitioner to English Sewing Limited is subject to a 15% withholding tax rate, portions of said ruling are quoted hereunder, thus:

> "In reply, please be informed that Article 11 of the RP-UK Tax Treaty provides:
>
> "Royalties
>
> "(1) Royalties arising in a Contracting State which are derived and beneficially owned by a resident of the other Contracting State may be taxed in that other state.
>
> 2. Such royalties may also be taxed in the Contracting State in which they arise, and according to the laws of that State. However, the tax so charged shall not exceed:

> (a.) 15 percent of the gross amount of the royalties, where the royalties are paid by an enterprise registered with the Philippine Board of Investments and engaged in preferred areas of activities, and also royalties in respect of cinematograph films and films tapes for television or radio broadcasting.
>
> (b.) in all other cases, 25 percent of the gross amount of the royalties
>
> xxx xxx xxx
>
> It is clear from the quoted tax treaty provision that when the payee is a BOI registered enterprise engaged in a preferred area of activity, such as ATCI, the applicable tax rate on its royalty payments is 15%.
>
> Considering the foregoing, your opinion that the 15% preferential tax rate under Article 11(b)(i) of the RP-UK Tax Treaty applies to gross royalty payments to English Sewing Ltd. is hereby confirmed.

We find the aforementioned evidence as well as the other documents offered by the petitioner sufficient to establish its entitlement to the claimed refund. However, in the final computation of the refundable amount, We had to disallow the payment made on November 25, 1994 due to prescription considering that the petition for review was filed on November 27, 1996 making said payment fall outside the two-year prescriptive period for claiming a refund pursuant to Section 230 of the Tax Code.

In summary, petitioner is entitled to the amount of P5,634,059.75 computed in detail as follows:

Filing Date	Amount	25% Tax Paid	Exh.
12-26-94	₱ 2,183,956.00	₱ 545,989.00	D
1-25-95	2,324,689.00	581,172.00	E
2-27-95	2,557,709.00	639,427.00	F
3-27-95	2,744,098.00	686,025.00	G
4-25-95	2,841,616.00	710,404.00	H
5-25-95	2,381,176.00	595,294.00	I
6-26-95	2,679,483.00	669,871.00	J
7-25-95	3,187,315.00	796,829.00	K
8-25-95	2,492,487.00	623,122.00	L
9-25-95	2,525,598.00	631,400.00	M
10-25-95	2,910,540.00	727,635.00	N
11-27-95	2,902,377.00	725,594.00	O
12-26-95	1,980,146.00	495,037.00	P
1-25-96	1,698,649.00	424,662.00	Q
2-26-96	2,349,302.00	587,326.00	R
3-25-96	2,495,153.00	623,788.00	S
4-25-96	2,728,437.00	682,129.00	T
5-27-96	1,580,662.00	395,146.00	U
6-25-96	1,899,973.00	474,993.00	V
7-25-96	2,528,709.00	632,177.00	W
8-26-96	2,211,767.00	552,942.00	X
9-25-96	2,351,834.00	587,959.00	Y
10-25-96	2,784,899.00	696,225.00	Z
TOTAL	₱56,340,575.00	₱14,085,146.00	
Multiply by	15%		
Should be taxed	8,451,086.25		
Less: Payments made	14,085,146.00		
Refundable	₱ 5,634,059.75		

WHEREFORE, in view of the foregoing, respondent Commissioner of Internal Revenue is hereby **ORDERED** to **REFUND** to petitioner the sum of ₱5,634,059.75 representing overpaid withholding tax on royalty payments for the period October 1994 to September 1995.

SO ORDERED.

ERNESTO D. ACOSTA
Presiding Judge

WE CONCUR:

RAMON O. DE VEYRA
Associate Judge

AMANCIO Q. SAGA
Associate Judge

CERTIFICATION

I hereby certify that this decision was reached after due consultation with 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