REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

SECOND DIVISION

CHINA BANKING CORPORATION,
Petitioner,

C.T.A. CASE NO. 6379

Members:

- versus -

CASTAÑEDA, JR., *Chairman*
UY, and
PALANCA-ENRIQUEZ, *JJ.*

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:
FEB 23 2005

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DECISION

UY, *J.*:

This is a petition for review of the Decision dated December 6, 2001 rendered by respondent, Commissioner of Internal Revenue, reiterating Assessment Notice Nos. FAS-5-82/85-89-000586 and FAS-5-86-89-000587 and finding petitioner liable to pay the aggregate amount of **Eleven Million Three Hundred Eighty Three Thousand One Hundred Sixty Five And 50/100 Pesos (P11,383,165.50)**, plus increments accruing thereon, representing deficiency documentary stamp taxes for the calendar years 1982 to 1986.

THE FACTS

Petitioner, China Banking Corporation, is a universal banking institution duly organized and existing in accordance with the laws of the Philippines with principal office at 8745 Paseo de Roxas corner Villar St., Makati City, while respondent is the duly appointed Commissioner of the Bureau of Internal Revenue (BIR) and may be duly served with summons and other court processes at his office at the BIR Building, East Triangle, Diliman, Quezon City.

During the periods from 1982 to 1986, petitioner was engaged in transactions involving sales of foreign exchange, or commonly known as SWAP transactions, to the then Central Bank of the Philippines, now Bangko Sentral ng Pilipinas or BSP for short.

On April 19, 1989, petitioner received a letter from respondent signed by Asst. Commissioner for Collection, Mr. Pedro G. Aguillon, dated April 11, 1989, with attached Income Tax Assessment Notice, thereby assessing petitioner the total amount of Php150,223.45 and Php11,383,165.50, representing its alleged deficiency expanded withholding tax at source and documentary stamp tax, respectively, on its SWAP Transactions/Arrangements for the taxable years 1982 to 1986, detailed as follows:

ON SWAP TRANSACTIONS FOR CALENDAR YEARS 1982 TO 1986

Deficiency Withholding Tax At Source

		Amount
Deficiency Withholding Tax Due		P 83,346.47
Add: 25% Surcharge		20,836.62
14% Interest from 1-26-85 to 12-31-85		10,855.97
20% Interest from 1-1-86 to 3-10-89		35,184.39
		P 150,223.45

Deficiency Documentary Stamp Tax

For the years 1982 to 1985		P 8,280,696.00
For calendar year 1986	P2,481,975.60	
Add: Surcharge	620,493.90	3,102,469.50
		P 11,383,165.50

(FAS-1-82/86-89-000585-587, Exhibit "A" and annexes, Records, pp. 145 – 147).

On May 8, 1989, petitioner, through its First Vice President (now Executive Vice President and Chief Operating Officer) Mr. Ricardo R. Chua, sent a letter of protest to respondent detailing therein reasons why it disagreed with the findings of respondent *(Exhibit "B", Records, pp. 148-150)*.

On December 21, 2001, petitioner received respondent's Decision, promulgated on December 6, 2001, canceling and withdrawing the assessed deficiency withholding tax at source in the amount of P150,223.45 for the taxable years 1982-1986 under Assessment Notice No. FAS-1-82/86-89-000585, but reiterating the assessed deficiency documentary stamp tax for the same calendar years covered under Assessment Notice Nos. FAS-5-82/85-89-00586 and FAS-5-86-89-000587 in the aggregate amount of P11,383,165.50, plus increments that may accrue thereon.

In resolving the validity of the assessments for the deficiency documentary stamp taxes, respondent relied on the following grounds, to wit:

> *"As regards the first issue, We resolve in the affirmative. It is clear from the aforecited Section 231 (subsequently renumbered as Section 195, now Section 182) of the Tax Code that foreign bills of exchange and letters of credit (including orders by telegraph or otherwise) for the payment of money drawn in but payable out of the Philippines are subject to documentary stamp tax. Accordingly, the documentary stamp tax prescribed by then Section 231 of the Tax Code is due and payable on the order covering the forward transaction as well as the order covering or leading to the spot sale of foreign exchange and not the document embodying the "Offer to Sell Spot Exchange under SWAP Arrangement" or the sale or purchase of foreign exchange which is not subject to the documentary stamp tax. The real parties to the SWAP transaction are the local bank as drawer and the former's foreign corresponding bank as drawee/acceptor.*
>
> *Pursuant to Section 222 (now Section 173) of the Tax Code, the documentary stamp tax is payable indifferently by either party making, signing, issuing, accepting or transferring the taxable document, hence, since the drawee (local bank's correspondent bank) is outside the taxing jurisdiction, the drawer local bank (China Banking Corporation) is liable to pay the documentary stamp tax on the aforementioned order. Furthermore, the flow of funds abroad from the Philippines to a foreign country is irrelevant to the accrual of the documentary stamp tax. The liability of an instrument to documentary stamp tax and the amount of tax are determined by the form and face thereof and cannot be affected*

by proofs of facts outside of the instrument itself (U.S. vs. Isham, 17 Wall. 496, 84 U.S. 496). The factual question whether or not there was a flow of fund from one country to another requires proof of facts outside the instrument itself. Be that as it may, however, where there is no fund or credit against an instrument is drawn, the said order would not be accepted or honored and there is no consummated transaction to speak of subject to DST (comments on the BAP Memo of May 18, 1987 to the BIR by Jose J. Santos, Chief, Franchise and Miscellaneous Tax Division)" (BIR DECISION, Exhibit "C", Records, pp. 151- 154)

Hence, this Petition for Review filed on January 18, 2002.

THE ISSUES

Petitioner and respondent stipulated the following as the issues of this case:

(1) Whether or not the transactions involving sales of foreign exchange commonly known as SWAP Arrangements should be treated as telegraphic transfer subject to documentary stamp tax under then Section 195 (now 182) of the Tax Code;

(2) Whether or not it is the Central Bank of the Philippines (now BSP) is the one liable for the DST assessed, if any party is liable;

(3) Whether or not petitioner was formally apprised of the sources and how the amounts indicated in the assessment were arrived at.

PETITIONER'S CLAIMS

Petitioner argues that its SWAP Arrangements may not be taxed as a telegraphic transfer under the then Section 195 of the National Internal Revenue Code (now Section 182) since if the local bank advises the correspondent foreign bank to turn over to the Federal Reserve Bank of the United States a specific amount in dollars corresponding to the SWAP for credit to the account of the Central Bank of the Philippines (now Bangko Sentral ng Pilipinas or BSP), payment is made in the Philippines. This contrasts with a telegraphic transfer where a foreign bank is instructed by a local bank to make payment also abroad, where such foreign bank is located.

Further, petitioner contends that, on the assumption that SWAP arrangement is a taxable transaction, it is the Central Bank of the Philippines which is liable for the tax liability under Sections 186 and 195 (now Sections 173 and 182, respectively) of the Tax Code; and that the tax and duty exemption of the Central Bank of the Philippines had been expressly withdrawn and revoked under Presidential Decree Nos. 1177 (July 30, 1977) and 1931 (June 11, 1984) and thus, for this reason, it is the one directly liable for the documentary stamp tax on the sale of foreign bills of exchange executed by petitioner to it during the periods of 1982 to 1986. Consequently, unless it could be shown that the exemption privileges of the Central Bank of the Philippines had been restored upon the recommendation of the Fiscal Incentives Review Board, herein petitioner then cannot be held liable for the subject deficiency documentary stamp tax. Excerpts from the Memorandum dated March 17, 1987 *(Exhibit "R")* of the Banker's Association the Philippines addressed to all member banks were quoted by petitioner to further bolster its claim that it is the Central Bank of the Philippines which is liable to pay the documentary stamp tax on the SWAP transactions, if such is payable at all.

RESPONDENT'S DEFENSES

Respondent, on the other hand, contends that documentary stamp taxes are levied on the exercise by persons of certain privileges conferred by law for the creation, revision or termination of specific legal relationships through the execution of specific instruments. Documentary stamp taxes are thus levied on the exercise of these privileges through the execution of specific instruments, independently of the legal status of the transactions giving rise thereto. The documentary stamp taxes must be paid upon the issuance of the said instruments, without regard to whether the contracts give rise to them are rescissible, void, voidable or unenforceable (Philippine Home Insurance Corporation, et. al. vs. CA and CIR, G.R. No. 119446, January 21, 1999).

It is the position of the respondent that when the local bank sells a foreign exchange (spot sale) in a SWAP Arrangement and the said local bank orders its correspondent bank abroad to remit the dollars to the correspondent bank of the Federal Reserve Bank, said order is considered a telegraphic transfer subject to the DST under the then Section 195 (now Section 182) of the Tax Code, as amplified by Sections 50 and 51 of Revenue Regulations No. 26, otherwise known as the Documentary Stamp Tax Regulations.

Furthermore, respondent argues that the flow of funds abroad from the Philippines to the United States is irrelevant to the accrual of the DST. The liability of an instrument to the documentary stamp tax and the amount of tax are determined by the form and face thereof and cannot be effected by proofs of facts outside of the instrument itself (U.S. vs. Isham, 17 Wall. 496, 84 U.S. 496). The then Section 195 (now Section 182) of the Tax Code subjects to DST foreign bills of exchange and letters of credit (including orders by telegraph or otherwise) for the payment of money drawn in but payable out of the Philippines. Thus, the DST prescribed by Section 195 of the Tax Code, as amended, is due and payable on the order covering the forward transaction as well as the order covering or leading to the spot sale of foreign exchange and not on the sale or purchase of foreign exchange, which are not subject to the DST.

In the case at bar, the real parties to the transaction are the local bank as drawer, which has a SWAP arrangement with the Central Bank, and the former's foreign corresponding bank as drawee/acceptor. Pursuant to the then Section 222 (now Section 178) of the Tax Code, the DST is payable indifferently by either party making, signing, issuing, accepting or transferring the taxable instrument. Hence, since the drawee (local bank's foreign correspondent bank) is not within the Philippine Government's taxing jurisdiction, the drawer local bank is liable to pay the DST on the aforementioned orders, any market convention to the contrary notwithstanding. And with the amendment of Section 222 of the Tax Code by Presidential Decree No. 1994 effective January 1, 1986, respondent concludes that the liability of the local bank, as drawer, for the DST on the order/cable instruction effected under the SWAP agreement becomes more explicit.

THIS COURT'S RULING

The disputed assessment in the case at bar pertains to deficiency documentary stamp taxes for the amount of **Eleven Million Three Hundred Eighty Three Thousand One Hundred Sixty Five And 50/100 Pesos (P11,383,165.50)** plus increments accruing thereon, for the calendar years 1982 to 1986 arising from the SWAP transactions entered into by petitioner with the then Central Bank of the Philippines (now Bangko Sentral ng Pilipinas or BSP for short).

The legal issue presented is not novel, as the same has already been ruled upon in the affirmative in a long line of decisions of this Court, duly affirmed by the Court of Appeals (when decisions of this Court were still reviewable by the said appellate court).

Principally, the question is, whether or not, transactions involving sales of foreign exchange commonly known as SWAP arrangements should be treated as telegraphic transfer subject to documentary stamp tax under then Section 195 (now 182) of the Tax Code.

In a SWAP agreement, a local bank, such as petitioner in the case at bar, enters into a contract and sells spot to the Bangko Sentral ng Pilipinas or BSP for short (formerly Central Bank of the Philippines), at the guiding rate/cross rate with the stipulation that at a future date, would purchase the same amount of foreign exchange from the BSP, upon maturity date of the SWAP agreement, at a specified rate. Two phases of the transaction are involved: (1) spot sale of foreign exchange by the local bank to the BSP; and (2) the forward (future) purchase by the local bank of the same amount of foreign exchange from the BSP, in both cases at agreed rates. The foreign exchange - subject matter of the swap arrangement, (US dollars in the case at bar), originates from a foreign bank where the local bank maintains a deposit, or is a grantee of a credit line for loan availments. The local bank advises the foreign bank to remit the dollar amount of swap to the Federal Reserve Bank for credit to the account of the BSP.

The order or cable instruction of the local bank to its foreign correspondent bank to remit a specific sum in dollars/foreign exchange to the Federal Reserve Bank for credit to the account of the BSP is considered a telegraphic transfer subject to the documentary stamp tax under then Section 195 (now Section 182) of the Tax Code. Said Section provides as follows:

> "**Sec. 195. Stamp Tax on Foreign Bills of Exchange and Letters of Credit -** On all foreign bills of exchange and letters of credit (**<u>including orders, by telegraph or otherwise, for the payment of money issued by express or steamship companies or by any person or persons</u>**) drawn in but payable out of the Philippines in a set of three (3) or more according to the custom of merchants and brokers, there shall be collected a documentary stamp tax of Thirty centavos (P0.30) on each Two hundred pesos (P200), or fractional part thereof, of the face value of any such bill of exchange or letter of credit, or the Philippine equivalent of such face value, if expressed in foreign currency." (emphasis supplied)

This provision is amplified by Section 51 of Revenue Regulations No. 26, otherwise known as the Documentary Stamp Tax Regulations, which reads thus:

> "**Section 51. What may be considered as telegraphic transfers.** – If a local bank cables to a certain bank in a foreign country with which bank said local bank has a credit, and directs that foreign bank to pay to another bank or person in the same locality a certain sum of money, the document for and in respect of such transaction will be regarded as a telegraphic transfer, taxable under the provisions of Section 1449(i) of the Administrative Code."

In the light of the foregoing legal provisions, it is clear that the imposition of documentary stamp tax in Section 195 (now Section 182) of the Tax Code is not limited only to foreign bills of exchange or letters of credit, but to all the orders made by telegraph, or by any other means, for the payment of money, to any person or persons drawn in but payable out of the Philippines. Thus, the cabled instructions of petitioner to its foreign correspondent bank to pay money falls within the ambit of Section 195 (now Section 182) of the Tax Code, the applicable law at the time of the SWAP agreements in question were transacted.

All the elements for a telegraphic transfer are indeed present, namely: (1) Petitioner bank cables its correspondent bank in the United States; and (2) Petitioner bank directs that correspondent bank to remit the dollar amount to the Federal Reserve Bank of the United States for credit to the account of the Central Bank of the Philippines (BSP).

Having resolved that Swap Agreements or arrangements are considered as telegraphic transfers and are therefore, subject to documentary stamp taxes, We now resolve the issue as to whether the petitioner is liable to pay such taxes covering the taxable years 1982 to 1986, including interest and surcharges.

Petitioner offered in evidence the testimony of its witness explaining the full description of a typical SWAP cycle. According to petitioner, the documentary stamp taxes have already been deducted from it at the end of the SWAP cycle by the Central Bank of the Philippines. Hence, petitioner should be deemed to have paid for such tax. Consequently, at the start of the SWAP cycle, and being consistent with the procedure that it is the buyer of foreign exchange who should shoulder the payment of the tax, which in this case is the Central Bank of the Philippines, then petitioner should not be made liable to pay at all.

This Court cannot agree with petitioner's contentions.

Then Section 222 of the Tax Code of 1977 clearly provides that:

> "**Section 222. Stamp taxes upon documents, instruments, and papers.** – Upon documents, instruments, and papers, and upon acceptance, assignments, sales, and transfers of the obligation right, or property incident thereto, there shall be levied, collected and paid, for and in respect of the transaction so had or accomplished, the corresponding documentary stamp taxes prescribed in the following sections of this Title, by the person making, signing, accepting, or transferring the same, and at the time such act is done or transaction had."

Based on the above-mentioned provision, there is no question that the documentary stamp tax is payable by either the person making, signing, issuing, accepting, or transferring the document, instrument or paper. Said provision leaves the tax to be paid indifferently by either party **(Sta. Clara Lumber Company, Inc. vs. Jose Aranas, C.T.A. Case No. 502, June 12, 1959)**.

In this case, since the party supposedly liable to pay the proper documentary stamp tax by market convention is a tax-exempt entity, it is thus justified that petitioner should pay for the taxes due considering that it is the one who transferred or sold the foreign bills of exchange. Moreover, "(a) documentary stamp tax is in the nature of an excise tax. Documentary stamp tax is not imposed upon the business transacted, but rather, it is imposed upon the privilege, opportunity or facility offered at exchanges for the transaction of the business" (**Commissioner of Internal Revenue vs. Herald Lumber Co., L-16340, February 29, 1964**).

In other words, any one of the parties (petitioner or Central Bank) can be made liable to pay for the documentary stamp tax. However, the Central Bank is a tax exempt entity. Consequently, since the Central Bank, as the party liable to the taxable document enjoys a tax exemption, the other party thereto who is not exempt, petitioner bank in this case, shall be the one directly liable for the tax.

Additionally, even the Bankers Association of the Philippines, to which petitioner is a member, affirmed that the party liable to pay the taxes, if tax-exempt, should **assume** the responsibility to pay such tax. And to quote certain comments as found in the same Memorandum issued by the Bankers Association of the Philippines to the Bureau of Internal Revenue thru the BIR-BAP Tax Committee dated September 29, 1987:

> *"The BAP contends that since the CB is the buyer in the spot sale of foreign exchange by telegraphic transfer, the CB perforce should pay for the corresponding DST. Did CB, in fact, pay the DST on the spot sale of foreign exchange as buyer thereof? CB under Section 130, of its charter, is exempt from all national, provincial, municipal, and city taxes and assessments. Certainly, the local bank cannot be made to pay twice on the same swap agreement, both on the spot sale and forward purchase. In the former, the local bank is the seller; in the latter, it is the buyer. It has been ruled by the Bureau of Internal Revenue that where the deed of absolute sale specifies, among others, that the buyer/vendee* ***assumes*** *the payment of the documentary stamp tax (DST) and by virtue of P.D. 1448, it is exempted from all taxes, etc., the buyer/vendee is therefore, exempt from paying the DST on the aforementioned deed of sale. (Letter to Philippine Convention Bureau dated July 19, 1984) Likewise, in* Ruling No. 097-79, *dated October 31, 1979, the BIR ruled that if under the terms of the contract you* ***assumed*** *the payment of the DST and thereby becomes directly liable for the tax, the said document is exempt from the DST in view of your exemption under P.D. 87. Ruling No. 140-79 dated December 27, 1979, similarly states so." (BAP Memorandum to The Commissioner of Internal Revenue, p 88, BIR Records) (e*mphasis supplied)

Unfortunately, petitioner failed to show proof that the Central Bank indeed assumed the responsibility for the payment of the documentary stamp taxes. Petitioner as a party to the transaction can therefore be legally assessed for deficiency documentary stamp taxes on its SWAP transactions.

The last issue is likewise resolved in the affirmative as this Court is convinced that petitioner was formally apprised of the sources and how the amounts indicated in the assessment were arrived at.

Evidently, petitioner was notified and requested by herein respondent for an informal conference with regard to its SWAP arrangement facilities with the Central Bank of the Philippines. In fact, on two occasions (Letter dated September 24, 1986 answering respondent's letter dated September 18, 1986, and the second Letter dated November 20, 1986 replying to respondent's Pre-assessment Notice dated November 13, 1986), petitioner informed respondent that it was sending its authorized representative, Mr. Diolan Monteleyola to attend and confer with respondent's representatives on its behalf *(BIR Records, pp. 36 and 66).*

Moreover, records would show that petitioner was able to assail in its Protest Letter dated May 8, 1989 to respondent, the latter's assessment for deficiency documentary stamp taxes. Petitioner cannot therefore say that it was not afforded due process as there was indeed proper notification on the part of respondent to petitioner.

WHEREFORE, in view of the foregoing, the subject Petition for Review is **DENIED** for lack of merit. Accordingly, Assessment Notice Nos. FAS-5-82/85-89-00586 and FAS-5-86-89-00587 for deficiency Documentary Stamp Taxes for the period from 1982 to 1986 are hereby **AFFIRMED**. Petitioner is **ORDERED TO PAY** herein respondent the amount of **ELEVEN MILLION THREE HUNDRED EIGHTY THREE THOUSAND ONE HUNDRED SIXTY FIVE AND 50/100 PESOS (P11,383,165.50)** plus 20% delinquency interest from January 20, 2002 up to the time such amount is fully paid.

SO ORDERED.

ERLINDA P. UY
Associate Justice

We Concur:

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Associate Justice

OLGA PALANCA-ENRIQUEZ
Associate Justice

CERTIFICATION

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

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Chairman