REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

EN BANC

SAL OPPENHEIM JR. & CIE KOMMANDITGESELLSCHAFT AUF AKTIEN,
Petitioner,

- versus -

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

CTA EB No. 906
(CTA Case No. 7923)

Present:

Del Rosario, *PJ*,
Castañeda, Jr.,
Bautista,
Uy,
Casanova,
Fabon-Victorino,
Mindaro-Grulla,
Cotangco-Manalastas, and
Ringpis-Liban, *JJ.*

Promulgated:

MAR 03 2014 Apolinario 9:00 a.m.

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AMENDED DECISION

COTANGCO-MANALASTAS, J.:

For resolution is petitioner's *Motion for Reconsideration (Re: Decision dated August 15, 2013)*[1] filed on September 20, 2013. Respondent failed to file her comment despite notice.

Petitioner seeks the reconsideration of this Court's Decision[2], promulgated on August 15, 2013, which dismissed the instant petition for review for lack of merit, thereby affirming the Decision dated February 27, 2012 and Resolution dated April 30, 2012 of the former Second Division denying petitioner's claim for refund or issuance of tax credit certificate representing overpaid final withholding tax on dividends.

[1] *Rollo*, pp. 265-275.
[2] *Rollo*, pp. 246-258.

Petitioner requests the reconsideration of this Court's Decision in light of the recent Supreme Court pronouncement in *Deutsche Bank AG Manila Branch vs. Commissioner of Internal Revenue*[3] which upheld the rights of qualified foreign entities to avail of the preferential tax treaty rates despite non-compliance with Revenue Memorandum Order (RMO) No. 1-2000. In the said case, the Supreme Court held that the respondent, in the exercise of her power to issue administrative regulations, cannot subject the availment of incentives under tax treaties to onerous requirements which are not contemplated under these international covenants. The High Court thus declared that the failure to file a tax treaty relief application (TTRA), as mandated under RMO No. 1-2000, should not preclude qualified taxpayers from enjoying applicable tax treaty benefits.

The instant motion for reconsideration is meritorious.

In the case of *Deutsche Bank AG Manila Branch vs. Commissioner of Internal Revenue*[4] *(Deutsche Bank* case*)*, the Supreme Court finally laid to rest the issue of whether the failure to file a TTRA prior to the transaction would deprive the taxpayer of the benefit of a tax treaty. The Supreme Court held that non-compliance with the prior application rule as required by RMO No. 1-2000 should not operate to automatically divest entitlement to the tax treaty relief as it would constitute a violation of the duty required by good faith in complying with a tax treaty and would impair the value of the tax treaty, *to wit*:

> "Our Constitution provides for adherence to the general principles of international law as part of the law of the land. The time-honored international principle of *pacta sunt servanda* demands the performance in good faith of treaty obligations on the part of the states that enter into the agreement. Every treaty in force is binding upon the parties, and obligations under the treaty must be performed by them in good faith. More importantly, treaties have the force and effect of law in this jurisdiction.
>
> Tax treaties are entered into 'to reconcile the national fiscal legislations of the contracting parties and, in turn, help the taxpayer avoid simultaneous taxations in two different jurisdictions.' *CIR v. S.C. Johnson and Son, Inc.* further clarifies that 'tax conventions are drafted with a view towards

[3] G.R. No. 188550, August 19, 2013.
[4] *Ibid.*

the elimination of international juridical double taxation, which is defined as the imposition of comparable taxes in two or more states on the same taxpayer in respect of the same subject matter and for identical periods. The apparent rationale for doing away with double taxation is to encourage the free flow of goods and services and the movement of capital, technology and persons between countries, conditions deemed vital in creating robust and dynamic economies. Foreign investments will only thrive in a fairly predictable and reasonable international investment climate and the protection against double taxation is crucial in creating such a climate.' Simply put, tax treaties are entered into to minimize, if not eliminate the harshness of international juridical double taxation, which is why they are also known as double tax treaty or double tax agreements.

'A state that has contracted valid international obligations is bound to make in its legislations those modifications that may be necessary to ensure the fulfillment of the obligations undertaken.' Thus, laws and issuances must ensure that the reliefs granted under tax treaties are accorded to the parties entitled thereto. **The BIR must not impose additional requirements that would negate the availment of the reliefs provided for under international agreements.** More so, when the RP-Germany Tax Treaty does not provide for any pre-requisite for the availment of the benefits under said agreement.

Likewise, it must be stressed that **there is nothing in RMO No. 1-2000 which would indicate a deprivation of entitlement to a tax treaty relief for failure to comply with the 15-day period.** We recognize the clear intention of the BIR in implementing RMO No. 1-2000, but **the CTA's outright denial of a tax treaty relief for failure to strictly comply with the prescribed period is not in harmony with the objectives of the contracting state to ensure that the benefits granted under tax treaties are enjoyed by duly entitled persons or corporations.**

Bearing in mind the rationale of tax treaties, **the period of application for the availment of tax treaty relief as required by RMO No. 1-2000 should not operate to divest entitlement to the relief as it would constitute a violation of the duty required by good faith in complying with a tax treaty. The denial of the availment of tax relief for the failure of a taxpayer to apply within the prescribed period under the administrative issuance would impair the value of the tax treaty.** At most, the application for a tax treaty relief from the BIR should merely operate to confirm the entitlement of the taxpayer to the relief.

> **The obligation to comply with a tax treaty must take precedence over the objective of RMO No. 1-2000**. Logically, noncompliance with tax treaties has negative implications on international relations, and unduly discourages foreign investors. While the consequences sought to be prevented by RMO No. 1-2000 involve an administrative procedure, these may be remedied through other system management processes, e.g., the imposition of a fine or penalty. But we cannot totally deprive those who are entitled to the benefit of a treaty for failure to strictly comply with an administrative issuance requiring prior application for tax treaty relief." (Emphasis supplied)

In the same case, the Supreme Court also held that prior application with the BIR becomes moot in refund cases and explained the rationale as follows:

> "Again, RMO No. 1-2000 was implemented to obviate any erroneous interpretation and/or application of the treaty provisions. The objective of the BIR is to forestall assessments against corporations who erroneously availed themselves of the benefits of the tax treaty but are not legally entitled thereto, as well as to save such investors from the tedious process of claims for a refund due to an inaccurate application of the tax treaty provisions. However, as earlier discussed, noncompliance with the 15-day period for prior application should not operate to automatically divest entitlement to the tax treaty relief especially in claims for refund.
>
> **The underlying principle of prior application with the BIR becomes moot in refund cases, such as the present case, where the very basis of the claim is erroneous or there is excessive payment arising from non-availment of a tax treaty relief at the first instance. In this case, petitioner should not be faulted for not complying with RMO No. 1-2000 prior to the transaction. It could not have applied for a tax treaty relief within the period prescribed, or 15 days prior to the payment of its BPRT, precisely because it erroneously paid the BPRT not on the basis of the preferential tax rate under the RP-Germany Tax Treaty, but on the regular rate as prescribed by the NIRC. Hence, the prior application requirement becomes illogical. Therefore, the fact that petitioner invoked the provisions of the RP-Germany Tax Treaty when it requested for a confirmation from the ITAD before filing an administrative claim for a refund should be deemed substantial compliance with RMO No. 1-2000.**
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> Corollary thereto, Section 229 of the NIRC provides the taxpayer a remedy for tax recovery when there has been an

> erroneous payment of tax. **The outright denial of petitioner's claim for a refund, on the sole ground of failure to apply for a tax treaty relief prior to the payment of the BPRT, would defeat the purpose of Section 229**." (Emphasis supplied)

Applying the foregoing pronouncement in this case, the fact that petitioner filed a TTRA before the International Tax Affairs Division, though belatedly, before filing an administrative claim for a refund should be deemed substantial compliance with RMO No. 1-2000.

Having disposed of the issue on the prior application rule, this Court will now proceed to determine if petitioner is entitled to the 15% preferential tax rate provided in the RP-Germany Tax Treaty.

Article 10 of the RP-Germany Tax Treaty provides:

> "ARTICLE 10
> *Dividends*
>
> 1. Dividends paid by a company which is a resident of a Contracting State to a resident of the other Contracting State may be taxed in that other State.
>
> 2. However, such dividends may be taxed in the Contracting State of which the company paying the dividends is a resident, and according to the law of that State, but the tax so charged shall not exceed:
>
> (a) 10 per cent of the gross amount of the dividends if the recipient is a company (excluding partnerships) which owns directly at least 25 per cent of the capital of the company paying the dividends;
>
> (b) in all other cases, 15 per cent of the gross amount of dividends."

Based on the above provision, the Philippines may tax the dividends paid by a Philippine company to a resident of Germany at a rate not exceeding (a) 10% of the gross amount of dividends if the recipient is a company (excluding partnerships) which owns directly at least 25% of the capital of the company paying the dividends; and (b) in all other cases, 15% of the gross amount of dividends.

Based on the evidence on record, the Court in Division found that petitioner is entitled to the 15% preferential tax rate on its dividend income. Thus, *We* quote with approval the findings of the Court in Division, *to wit*:

> "Petitioner owns shares of stock in Philippine domestic corporations, including, among others, PLDT [Philippine Long Distance Telephone Company] shares of stock through BBH [Brown Brothers Harriman and Co.] and HSBC [Hongkong and Shanghai Banking Corporation]. BBH acts as petitioner's global custodian bank, facilitating the settlement of the purchase and sale of shares as well as the collection of dividends therefrom; while HSBC acts as BBH's sub-custodian in the Philippine market.
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> As testified to by Ms. Maria Katherine C. dela Torre, HSBC's Assistant Vice President of Custody and Clearing Department, the PLDT shares of stock owned by petitioner are scripless securities which are listed in the Philippine Stock Exchange, and they are not evidenced by a stock certificate, but instead they are represented by electronic records in the depository system of the Philippine Depository and Trust Corporation (PDTC). Hence, the PLDT shareholdings of BBH's clients (including petitioner's shares) are represented by electronic entries under BBH's Omnibus Securities Account No. 000-453332-569 with HSBC and these are also reflected in HSBC's Omnibus Account with PDTC (i.e., HSBC-Account 10), wherein the equity investments of all of HSBC's foreign clients are lodged.
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> The PSE adopted the scripless system whereby the settlement of purchases, sales of shares of stock and distribution of dividends are made through the electronic book entry system, rather than by the physical movement of certificates and documents.
>
> When PLDT declared dividends consisting of P50.00 per share of common stock to holders of record on March 20, 2007, which was payable on April 20, 2007 and P60.00 plus P40.00 per share of common stock to holders of record on August 24, 2007, which was payable on September 24, 2007, HSBC certified that petitioner held the following number of outstanding shares of PLDT stock as of the aforementioned dates:

EXH.	DATE	DIVIDEND PER SHARE	NO. OF SHARES	GROSS ENTITLEMENT	TAX AMOUNT (35%)	NET ENTITLEMENT
R-1	20-Mar-07	P 50.00	163,850	P 8,192,500.00	P 2,867,375.00	P 5,325,125.00
R-2	24-Aug-07	P100.00	126,970	12,697,000.00	4,443,950.00	8,253,050.00
TOTAL				**P20,889,500.00**	**P7,311,325.00**	**P13,578,175.00**

BBH likewise issued a Proof of Final Distribution of the subject dividends.

In turn, the corresponding withholding agent/payor filed Monthly Remittance Returns of Final Income Taxes Withheld (BIR Form No. 1601-F) for FWT withheld in the months of April and September 2007, detailed as follows:

EXHIBIT	DATE FILED	WITHHOLDING AGENT	TOTAL FWT REMITTED
L-1 and L	11-May-07	HSBC	P1,262,416,735.43
M-1 and M	15-Oct-07	PLDT	P2,656,843,465.84

Suffice it to state that not all holdings in the HSBC Custody Account are petitioner's holdings. Consequently, not all final taxes withheld are from the dividends received by petitioner on its shareholdings in PLDT.

As stipulated upon by the parties, the dividends received by petitioner were subjected to final withholding tax amounting to P7,311,325.00 pursuant to Section 28 (B) (1) of the NIRC of 1997, as amended, at the rate of 35% and that the same were remitted to the BIR by PLDT's transfer agent. Furthermore, the Revenue Accounting Division of the BIR issued certifications that it received the following payments:

EXHIBIT	DATE	TAXPAYER	FWT
CC	11-May-07	HSBC	P1,262,416,735.43
BB and BB-1	28-Sep-07	PLDT	P2,591,872,335.00
BB and BB-2	15-Oct-07	PLDT	P64,971,130.84

In order to bolster its entitlement to the preferential tax rate, petitioner submitted the following documents to prove that it is a resident of the Federal Republic of Germany:

1. Certificate of Non-Registration of Corporation/Partnership issued by the Securities and Exchange Commission;

2. Certificate of Residence for 2007 issued by the Tax Authority of the Federal Republic of Germany; and

3. Certificate of Residence for 2008 issued by the Tax Authority of the Federal Republic of Germany.

Petitioner filed an application to avail of the benefits of the RP-Germany Tax Treaty on February 12, 2009.

xxx xxx xxx

Petitioner asserts that based on the said treaty the applicable tax rate for the dividends it received should only be 15% since it only has the following shares of stock in the outstanding common shares of PLDT as of the following record dates:

Date	No. of Shares	Total number of PLDT Outstanding Common Shares (Exhibit "H")	Percentage of petitioner's shares
20-Mar-07	163,850	188,574,293	0.087%
24-Aug-07	126,970	188,707,593	0.067%

Petitioner is claiming the refund of the twenty percent (20%) difference between the tax rate imposed as FWT under Section 28 (B) (1) of the NIRC of 1997 and the 15% tax rate that allegedly should be applied under the RP-Germany Tax Treaty.

While petitioner is entitled to the 15% tax rate provided under the RP-German Tax Treaty...."

From the foregoing, considering that petitioner is a company which is a resident of Germany and does not hold directly at least 25% of the capital of PLDT, a domestic corporation, then the dividend payment of PLDT to petitioner is subject to 15% preferential tax rate based on the gross amount of the dividend, pursuant to Article 10 (2)(b) of the RP-Germany Tax Treaty. Consequently, since the dividends received by petitioner were subjected to 35% final withholding tax instead of the 15% preferential tax rate, then it is proper to grant petitioner a refund for the difference of P4,177,900.00 (P7,311,325.00 less P3,133,425.00).

As a final note, the Supreme Court, by tradition and in our system of judicial administration, has the last word on what the law is. It is the final arbiter of any justiciable controversy. There is only one Supreme Court from whose decisions all other courts should take their bearings.[5] Thus, this Court is obliged to apply the jurisprudence as enunciated in the *Deutsche Bank* case.

WHEREFORE, premises considered, the instant Motion for Reconsideration is hereby **GRANTED**. The Decision dated February 27, 2012 and Resolution dated April 30, 2012 of the former Second Division are hereby **REVERSED** and **SET ASIDE**. Accordingly, respondent is hereby **ORDERED** to **REFUND** or **ISSUE A TAX CREDIT CERTIFICATE** in favor of

[5] *Dante Nacuray et al. vs. NLRC, et al.,* G.R. Nos. 114924-27, March 18, 1997.

petitioner in the amount of **P4,177,900.00**, representing excess final withholding tax paid on dividends.

SO ORDERED.

AMELIA R. COTANGCO-MANALASTAS
Associate Justice

WE CONCUR:

ROMAN G. DEL ROSARIO
Presiding Justice

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

LOVELL R. BAUTISTA
Associate Justice

ERLINDA P. UY
Associate Justice

CAESAR A. CASANOVA
Associate Justice

ESPERANZA R. FABON-VICTORINO
Associate Justice

Cielito N. Mindaro-Grulla
CIELITO N. MINDARO-GRULLA
Associate Justice

Ma. Belen M. R. L.
MA. BELEN M. RINGPIS-LIBAN
Associate Justice

CERTIFICATION

Pursuant to Section 13, Article VIII of the Constitution, it is hereby certified that the above Decision has been reached in consultation with the members of the Court *En Banc* before the case was assigned to the writer of the opinion of the Court.

ROMAN G. DEL ROSARIO
Presiding Justice