REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

IBM PHILIPPINES, INCORPORATED,
Petitoner,

- versus - C.T.A. CASE NO. 4308

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

3/31/93

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D E C I S I O N

This is a claim for the refund of the amount of P29,223,638.94 representing allegedly overpaid withholding tax on royalties remitted by the petitioner to IBM WORLD WORLD TRADE CORPORATION, a non-resident foreign corporation, organized under the laws of the state of New York, U.S.A.

Petitioner is a domestic corporation organized and existing under the laws of the Philippines with principal office at IBM Building, Paseo de Roxas, Makati, Metro Manila. For the tax years 1986, 1987 and for the period January - July 1988, IBM World Trade has granted petitioner IBM Phils., a license, including the right to sublicense its (World Trade) subsidiaries under all patents, inventions, and copyrights and under all proprietary rights in programs, with respect to which patents, inventions, copyrights and proprietary the right to use its trade names and trademarks owned and/or registered in the name of World Trade. IBM World Trade in an Agreement dated September 1, 1982, had sublicensed to its subsidiary the said rights and likewise agreed to provide IBM Phils., its technical knowledge and know-how.

In consideration of such agreement, herein petitioner agreed to pay IBM World Trade royalties equivalent to 10% of the gross charges less returns and allowances, made during each calendar month by petitioner to its customers for the sale, service, lease and/or installation of IHS Products. The World Trade Agreement expired on August 31, 1987, extended the period of the grant for another five (5) years. This second agreement was approved by the Central Bank (Annexes "LL", "LL-1" and "LL-2). Petitioner IBM World Trade agreed to defer the provision with respect to Programs starting on January 1, 1988 (Annex "MM).

Hence, on January 1,1988 a new agreement with IBM World Trade, with respect to licensing of IBM Programs and access to and use of technical knowledge and know-how of IBM Programs, (Annex "NN"). Petitioner were likewise granted the right to use all of IBM's trademarks on or in association with IBM programs and to provide the petitioner with available technical knowledge and know-how relating to the reproduction, use, modification, marketability, education of users, services and maintenance of IBM Programs. For and in consideration of such agreement, petitioner agreed to pay IBM World Trade royalties equivalent to 40% of all its revenues, excluding discounts and other allowances, billed or accrued during each calendar month, on sale, service, lease, or installation of an IBM Program which petitioner authorized, license, or distributed to any affiliated party, or 40% of the price of one unit that petitioner would bill a third party for the licensing or authorizing to use IBM Programs for each copy of an IBM Program that petitioner uses internally.

For the tax years 1986, 1987 and during the period from January to July 1988, petitioner remitted royalties to IBM World Trade the sum of P194,822,459.77. The corresponding taxes on royalties were withheld thereon at the rate of 25% and remitted to the BIR in the sum of P48,705,614.92. However, on September 16, 1988, petitioner through its counsel Romulo Mabanta, Buenaventura Sayoc and De Los Angeles obtained from then, Commissioner of Internal Revenue Bienvenido A. Tan, Jr., BIR ruling No. 456-88 holding that "royalties arising in the Philippines and payable to World Trade as well as to IBM by IBM Phils. are subject to the Philippine tax at the rate of 10% because this rate appears in the RP - West Germany Tax Treaty and pursuant to Article 13, paragraph 2(b)(iii), of RP - US Tax Treaty. "(Annex "HH", pp. 73-76, C.T.A. Records).

Subsequently, in a letter dated October 15, 1988, petitioner through counsel, filed a claim for refund of excess taxes withheld in the amount of P29,223,368.94.

No responsive action on said claim, having been made by respondent and to interrupt the running of the 2 year period of prescription, petitioner appealed to this Court on November 2, 1988.

Respondent on the other hand, in his Answer, generally denies the material facts alleged in the petition for review and as special and affirmative defenses alleged, among others:

1. That petitioner is not the real party in interest;

2. That BIR Ruling dated September 16, 1988 invoked by petitioner does not in any way provide for the refund of the alleged overpaid tax withholding on the royalties; and

3. That petitioner has the burden of proving that it is entitled to the amount sought to be refunded, the claim being in the nature of an exemption from taxation, which cannot be made to rest on vague implications and must be construed strictly against petitioner.

The issues to be resolved in this case are as follows:

1. Whether or not petitioner has the legal capacity to institute this suit;

2. Whether or not petitioner should be taxed at the rate of 10% withholding tax on royalties in accordance with Article 12(2) of the R.P.- West Germany Tax Treaty and not 25% withholding tax on royalties under Article 13(2)(b)(iii) of the R.P.- U.S. Tax Treaty; and

3. Whether or not petitioner is entitled to the refund of P29,223,638.94, allegedly representing overpaid withholding tax on royalties.

It may not be amiss to state at this juncture, that the first issue is not new. The Supreme Court in the case of Commissioner of Internal Revenue vs. Procter & Gamble PMC, G.R. No. 66838, through a Resolution En Banc, dated December 2, 1991, in effect ruled that by a reasonable standard, the withholding agent, should be regarded as a party in interest, to bring suit for refund of taxes he believes were illegally collected from him. We quote at length from the said Resolution, to wit:

> "The term 'taxpayer' is defined in our NIRC as referring to <u>any person subject to tax</u> imposed by the Title (on Tax on income).' It thus becomes important to note that under Section 53 (c) of the NIRC, the withholding agent who is required to deduct and withhold any tax is made 'personally liable for such tax' and indeed is indemnified against any claims and demands which the stockholder might wish to make in questioning the amount of payments effected by the withholding agent in accordance with the provisions of the NIRC. The withholding agent, P & G - Phil., is <u>directly and indepently liable</u> for the correct amount of the tax that should be withheld from dividend remittances. The withholding agent is, moreover, subject to and liable for deficiency assessments, surcharges and penalties should the amount of the tax withheld be finally found to be less than the amount that should have been

> withheld be finally found to be less than the amount that should have been withheld under the law.

A person liable for tax has been held to be a person subject to tax and properly considered a 'taxpayer.' The term 'liable for tax' and 'subject to tax' both connote legal obligation or duty to pay a tax. It is very difficult, indeed conceptually impossible, to consider a person who is statutorily made 'liable for tax' as <u>not</u> 'subject to tax.' <u>By any reasonable standard, such a person should be regarded as a party in interest, or as a person having sufficient legal interest, to bring a suit for refund of taxes he believes were illegally collected from him.</u>

In <u>Philippine Guaranty Company, Inc. vs. Commissioner of Internal Revenue,</u>[1] this Court pointed out that a withholding agent is in fact the agent both of the government and of the taxpayer, and that the withholding agent is not an ordinary government agent:

> <u>'The law sets no condition for the personal liability of the withholding agent to attach.</u> The reason is to compel the withholding agent to withhold the tax under all circumstances. In effect, the responsibility for the collection of the tax as well as the payment thereof is

> concentrated upon the person over whom the Government has jurisdiction. Thus, the withholding agent is constituted the agent of both the Government and the taxpayer. With respect to the collection and/or withholding of the tax, he is the Government's agent. In regard to the filing of the necessary income tax return and the payment of the tax to the Government, he is the agent of the taxpayer. The withholding agent, therefore, is no ordinary government agent especially because under Section 53(c) he is held personally liable for the tax he is duty bound to withhold; whereas the Commissioner and his deputies are not made liable by law'.(Emphasis supplied)

If, as pointed out in Philippine Guaranty, the withholding agent is also an agent of the beneficial owner of the dividends with respect to the filing of the necessary income tax return and with respect to actual payment of the tax to the government, such authority may reasonably be held to bring an action for recovery of such claim. This implied authority is especially warranted where, as in the instant case, the withholding agent is the wholly owned subsidiary of the parent-stockholder and therefore, at all times, under the effective control of such parent-stockholder. In the circumstances of this case, it seems particularly unreal to deny the implied authority of P & G - Phil. to claim a refund and to commence an action for such refund.

We believe that, even now, there is nothing to preclude the BIR from requiring P & G - Phil. to show some written or telexed confirmation by P & G - USA of the subsidiary's authority to claim the refund or tax credit and to remit the proceeds of the refund, or to apply the tax credit to some Philippine tax obligation of, P & G - USA, <u>before actual payment of the refund or issuance of a tax credit certificate</u>. What appears to be vitiated by basic unfairness is petitioner's position that, although P & G - Phil. is directly and personally liable to the Government for the taxes and any deficiency assessments to be collected, the Government is not legally liable for a refund simply because it did demand a written confirmation of P & G - Phil.'s implied authority from the very beginning. A sovereign government should act honorably and fairly at all times, even <u>vis-a-vis</u> taxpayers.

We believe and so hold that, under the circumstances of this case, P & G - Phil. is properly regarded as 'taxpayers' within the meaning of Section 309, NIRC, and as impliedly authorized to file the claim for refund and the suit to recover such claim." (Underscoring supplied) The ruling is reiterated by the Supreme Court in the recent case of Commissioner of Internal Revenue vs. The Court of Tax Appeals, et al., G.R. No. 93901, February 11, 1992.

We find no cogent reason to deviate from the conclusion reached in the above-cited cases and the same should resolve the similar question presented in this appeal.

On the second issue, whether or not petitioner should be taxed at the reduced rate of 10% withholding tax on royalties in accordance with Article 12(2)(b) of the R.P.- West Germany Tax Treaty and not 25% withholding tax on royalties under Article 13(2)(b)(iii) of the R.P.- U.S. Tax Treaty.

This Court is of the persuasion that petitioner's stand is correct and concurs with the opinion rendered by then Commissioner of Internal Revenue, Bienvenido Tan, Jr. (BIR Ruling No. 456-88, supra., that under the most favored nation provision of the R.P.- U.S. Tax Treaty (Article 13, paragraph 2(b)(iii), the tax imposable on royalties derived by a resident of the United States from sources within the Philippines shall be the lowest rate of Philippine tax that may be imposed on royalties of the same kind paid under similar circumstances to a resident of a third state. Article 12, paragraph 2(b) of the R. P. - West Germany Tax Treaty, provides that royalties arising in the Philippines and paid to a resident of West Germany may also be taxed in the Philippines, but the tax so charged shall not exceed 10% of the gross amount of royalties. Said treaty also provides that for as long as the transfer of technology under Philippine law, is subject to approval, the limitation of the tax rate in case of royalties arising in the Philippines, apply if the contract giving rise to such royalties has been approved by Philippine competent authorities.

Thus, inasmuch as the Agreement between World Trade and IBM Phils. as well as the Agreement between IBM and IBM Phils. had been approved by the Central Bank of the Philippines, royalties arising in the Philippines and payable to World Trade as well as to IBM by IBM Phils. should be taxed at the rate of 10% because said rate is indicated in the R.P. - West Germany Tax Treaty and pursuant to Article 13, paragraph 2(b)(iii), of the RP - US Tax Treaty.

We now come to the third issue, whether or not petitioner is entitled to a tax refund of P29,223,638.94 representing the overpaid withholding tax on royalties.

To support its claim, petitioner presented evidences on the alleged amount sought to be refunded by submitting during the trial of this case, xerox copies of its monthly remittances, BIR Payment Orders and corresponding Confirmation Receipts issued by the Central Bank. It also submitted the corresponding vouchers charged by the affiliated company to prove that the royalties were actually paid.

After going over the evidences and evaluating the same, this Court finds that petitioner has indeed, overpaid the withholding tax on royalties, in the amount of P29,223,368.94, hence, entitled to the refund thereof, computed as follows:

1986	Amount of Royalties	Tax at 25%	Tax at 10%	Overpayment
Jan	P 3,279,429.79	P 819,857.45	P 327,942.98	P 491,914.47
Feb	4,075,596.30	1,018,899.08	407,559.63	611,339.45
Mar	3,452,590.26	863,147.57	345,259.03	517,888.54
Apr	3,939,978.08	984,994.52	393,997.81	590,996.71
May	3,493,334.63	873,333.65	349,333.46	524,000.19
Jun	3,470,970.96	867;742.73	347,097.10	520,645.64
Jul	6,727,309.32	1,681,827.33	672,730.93	1,009,096.40
Aug	3,328,769.82	832,192.45	332,876.98	499,315.47
Sep	3,600,960.80	900,240.20	360,096.08	540,144.12
Oct	4,512,731.60	1,128,182.90	451,273.16	676,909.74
Nov	5,611,346.52	1,402,836.63	561,134.65	841,701.98
Dec	13,616,114.25	3,404,028.56	1,361,611.43	2,042,417.14
1987				
Jan	P 2,649,659.28	P 662,414.82	P 264,965.93	P 397,448.89
Feb	3,287,762.49	821,940.62	328,776.25	493,164.37
Mar	2,877,533.16	719,383.29	287,753.32	431,629.97
Apr	5,557,488.07	1,389,372.02	555,748.81	833,623.21
May	4,517,231.57	1,129,307.89	451,723.16	677,584.74
Jun	8,519,056.65	2,129,764.16	851,905.67	1,277,858.50
Jul	9,089,402.58	2,272,350.65	908,940.26	1,363,410.39
Aug	4,487,046.17	1,121,761.54	448,704.62	673,056.93
Sep	2,411,699.60	602,924.90	241,169.96	361,754.94
Oct	7,201,796.59	1,800,449.15	720,179.66	1,080,269.49
Nov	3,396,659.14	849,164.78	339,665.91	509,498.87
Dec	16,064,846.72	4,016,211.68	1,606,484.67	2,409,727.01
1988				
Jan	P 7,369,014.68	P 1,842,253.67	P 736,901.47	P 1,105,352.20
Feb	6,087,162.88	1,521,790.72	608,716.29	913,074.43
Mar	14,065,961.98	3,516,265.49	1,406,506.20	2,109,759.30
Apr	5,385,411.59	1,346,352.90	538,541.16	807,811.74
May	6,635,729.60	1,658,932.40	663,572.96	995,359.44
June	19,133,298.89	4,783,324.73	1,913,329.89	2,869,994.83
July	6,977,465.80	1,744,366.45	697,746.58	1,046,619.87
	194,882,459.77	48,708,614.92	19,482,245.98	P29,223,368.94

WHEREFORE, respondent is hereby ordered to refund to petitioner the amount of P29,223,368.94, representing excess payments of withholding taxes on royalties, for the tax years 1986, 1987 and during the period from January to July 1988.

SO ORDERED

Quezon City, Metro Manila, March 31, 1993.

MANUEL K. GRUBA
Associate Judge

WE CONCUR :

ERNESTO D. ACOSTA
Presiding Judge

RAMON O. DE VEYRA
Associate Judge

CERTIFICATION

I hereby certify that this 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