REPUBLIC OF THE PHILIPPINES
Court of Tax Appeals
QUEZON CITY

Third Division

FLUOR DANIEL, INC. - PHILIPPINES, *Petitioner,*	**CTA CASE NO. 8444**
	Members:
-versus-	***Bautista,*** *Chairperson* ***Fabon-Victorino,*** *and* ***Ringpis-Liban, JJ.***
COMMISSIONER OF INTERNAL REVENUE, *Respondent.*	Promulgated: JUL 11 2016 10:30 a.m.

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DECISION

BAUTISTA, J:

THE CASE[1]

This is a Petition for Review filed in accordance with *Rule 4, Section 3(a)(1)*[2] *of the Revised Rules of the Court of Tax Appeals* ("RRCTA") appealing the Final Decision on Disputed Assessment ("FDDA") dated February 13, 2012 and seeking the cancellation and withdrawal of the assessed deficiency Final Withholding Tax ("FWT") in the amount of Php69,592,164.18 for taxable year 2008, inclusive of interest and penalties; and the refund or the issuance of a tax credit certificate ("TCC") in favor of petitioner, representing the portion of the deficiency FWT assessment, inclusive of interest, which was paid under protest in the amount of Php29,825,213.22.

THE PARTIES

[1] *Records, CTA Case No. 8444, Vol. I, Pre-trial Order ("PTO"),* p. 139.
[2] *A.M. No. 05-11-07-CTA,* November 22, 2005.

Petitioner Fluor Daniel, Inc. - Philippines is a domestic corporation duly organized and existing under and by virtue of the laws of the Republic of the Philippines, with principal office located at Asian Star Building, 2402-2404 ASEAN Drive, Muntinlupa City; and is registered with the Bureau of Internal Revenue ("BIR") under Tax Identification No. 000-159-649-000.[3] It is engaged in the business of providing detailed engineering design, procurement, controls and project management services for a wide range of projects applicable to industries such as electronics, petroleum and petrochemicals, pharmaceuticals and biotechnology.[4]

Respondent Commissioner of Internal Revenue ("CIR") is the government official duly charged with the duty of assessing and collecting internal revenue taxes and the power to cancel disputed assessments, with office address at the BIR National Office Building, BIR Road, Diliman, Quezon City.[5]

THE FACTS

On October 26, 2011[6], petitioner received a duly executed and authentic Formal Letter of Demand ("FLD")[7] with attached Final Assessment Notices ("FAN")[8], all dated October 5, 2011, assessing petitioner the alleged deficiency taxes in the total amount of Php634,418,443.46, inclusive of interest computed up to October 31, 2011 and the alleged deficiency FWT in the amount of Php43,038,190.32[9], exclusive of interest, on software maintenance service fees paid by petitioner to Fluor Intercontinental, Inc. ("FII") on the ground that the same constitutes royalties.[10] The assessment can be broken down as follows:

	BASIC	INTEREST	COMPROMISE PENALTY	TOTAL
INCOME TAX	P 10,361,919.41	P 5,274,642.81		P 15,636,562.22
VALUE-ADDED TAX	1,097,952.17	616,056.45	P 25,000.00	1,739,008.62
FINAL WITHHOLDING TAX	380,088,190.32	213,265,921.58		593,354,111.90
FINAL WITHHOLDING VAT	14,755,950.97	8,279,503.45		23,035,454.42
FRINGE BENEFIT TAX	418,492.10	234,814.20		653,306.30

[3] *Records, Vol. I, Joint Stipulation of Facts and Issues ("JSFI"), par. 1,* p. 130.
[4] *Id., Audited Financial Statements ("AFS"), Exhibit "P," Note 1,* p. 334.
[5] *Id., JSFI, par. 2,* pp. 130-131.
[6] *Id., Exhibit "A,"* p. 243.
[7] *Id., Exhibit "A,"* pp. 243-250.
[8] *Id., Exhibit "A,"* pp. 251-255.
[9] Php122,966,258.05 x 35%.
[10] *Records, Vol. I, JSFI, par. 3,* p. 131.

GRAND TOTAL	P 634,418,443.46

On November 15, 2011, petitioner filed its protest to the FLD.[11]

The parties entered into a Taxpayer's Agreement Form ("TAF"), wherein petitioner voluntarily bound itself to pay the amount of Php166,586,113.90,[12] broken down as follows:

		BASIC		INTEREST		COMPROMISE PENALTY		TOTAL
INCOME TAX	P	309,657.30	P	174,935.16			P	484,592.46
VAT					P	25,000.00		25,000.00
FINAL TAX ON DIVIDEND		84,262,500.00		51,988,808.22				136,251,308.22
FINAL TAX ON ROYALTIES		18,444,938.71		11,380,274.51				29,825,213.22
TOTALS	**P**	**103,017,096.01**	**P**	**63,544,017.89**	**P**	**25,000.00**	**P**	**166,586,113.90**

Payments in the total amount of Php166,586,113.90 were made to the BIR, as follows:

		AMOUNT	BIR FORM 0605	FILING DATE	PAYMENT DATE
INCOME TAX	P	484,592.46	*Exhibit* "E"[13]	February 8, 2012	February 10, 2012[14]
VAT		25,000.00	*Exhibit* "H"[15]	February 8, 2012	February 10, 2012[16]
FINAL TAX ON DIVIDEND		136,251,308.22	*Exhibit* "F"[17]	February 8, 2012	February 10, 2012[18]
FINAL TAX ON ROYALTIES		29,825,213.22	*Exhibit* "G"[19]	February 8, 2012	February 10, 2012[20]
TOTALS	**P**	**166,586,113.90**			

On February 22, 2012[21], petitioner received an authentic and duly executed FDDA[22] containing respondent's final decision on petitioner's protest.[23]

Thus, on March 23, 2012, petitioner filed the present Petition for Review.[24]

On March 28, 2012, respondent received a letter dated March 27, 2012 from petitioner with the advice that the latter already paid the

[11] *Records, Vol. I, Exhibit "B,"* pp. 256-277.
[12] *Id., Exhibit "D,"* pp. 281-282.
[13] *Id., Exhibit "E,"* pp. 283-284.
[14] *Id., Exhibit "E,"* pp. 285-287.
[15] *Id., Exhibit "H,"* pp. 298-299.
[16] *Id., Exhibit "H,"* pp. 300-302.
[17] *Records, Vol. I, Exhibit "F,"* pp. 288-289.
[18] *Id., Exhibit "F,"* pp. 290-292.
[19] *Id., Exhibit "G,"* pp. 293-294.
[20] *Id., Exhibit "G,"* pp. 295-297.
[21] *Id., Exhibit "C,"* p. 280.
[22] *Id., Exhibit "C,"* pp. 278-280.
[23] *Records, Vol. I, JSFI, par. 4,* p. 131.
[24] *Id., PFR,* pp. 6-56, with annexes.

foregoing amounts, including its payment under protest of the alleged FWT on royalties in the amount of Php29,825,213.22.[25]

On May 21, 2012, respondent filed her Answer[26] interposing the following Special and Affirmative Defenses:[27]

> Respondent hereby reiterates and repleads the preceding paragraphs of This Answer as part of her Special and Affirmative Defenses.
>
> 4. The assessment for deficiency [FWT] on Royalties in the amount of [Php]69,592,164.18 was issued in accordance with law and related revenue issuances. The software maintenance service fees paid by petitioner to [FII] constitute royalties.
>
> 5. Petitioner executed a contract with FII and based on its terms and conditions, the nature of the contract showed that: (a) FII does not transfer all its substantial rights in the software, (b) the transactions involve only the transfer of copyright rights in the software, (c) The transaction does not constitute a sale or exchange.
>
> 6. The following is the computation prepared by the examiner as a result of the investigation conducted:

FINAL WITHHOLDING TAX ON ROYALTIES
Assessment No. LTRAD3-WF-0001-08

Software Maintenance Service fee (Royalties) paid to [FII]	P	122,966,285.05
WF Rate		35%
Total	P	43,038,190.32
Less: Remittance per Return		-
Deficiency WF	P	43,038,190.32
Add: Interest		26,553,973.86
TOTAL DEFICIENCY WITHHOLDING TAX	**P**	**69,592,164.18**

> 7. The Petitioner emphasized the definition of the term Royalties under Section 3(a) but intentionally failed to consider Section 3 (b) of RMC No. 44-05 which provides that the "definition of royalties includes payments for the use of copyright over software."
>
> 7.1 Section 3 (b) of RMC No. 44-05 is quoted as follows:

[25] *Records, Vol. I, Exhibits "I" to "I-1," with annexes*, pp. 303-315.
[26] *Id., Answer*, pp. 65-75.
[27] *Id., Answer*, pp. 66-73.

> "(b) Definition of royalties includes payments for the use of copyright over software- Software is generally assimilated as a literary, artistic or scientific Work protected by the copyright laws of various countries. Thus, payments in consideration for the use of or the right to use a copyright relating to software are generally royalties."

8. Petitioner invoked After-Sales Service with regard to treatment of payments obtained in contracts for the use of software under RMC No. 44-05. However, there was no sales transaction pertaining to the use of software that occurred between the Petitioner and FII.

> 8.1 Section 5 (c) of RMC No. 44-05 is quoted as follows:
>
> "(c.) After-Sales Service. Contracts for the use of software are often accompanied with the provision of services (e.g., installation, maintenance, and customization of the software) by personnel of the relevant foreign licensor/owner or the relevant local subsidiary, reseller, and distributor. Payments as consideration for after-sales service in a mixed contract are not royalties alone, but will include income from services. The appropriate course to take with such a contract is, in principle, to break down, on the basis of the information contained in the contract or by means of a reasonable apportionment, the whole amount of the stipulated payments according to the various parts of what is being provided under the contract, and then apply to each part of it so determined the taxation treatment proper thereto. Thus, the part of the payments representing the use of the software will be treated as royalties and taxable as such [] and the other part of the payments representing the provision of services will be treated as income from services and taxable as such.
>
> If, however, one part of what is being provided constitutes by far the principal purpose of the contract and the other parts stipulated therein are only of an ancillary and largely unimportant character, then the treatment applicable to the

principal part should generally be applied to the whole amount of the consideration.

9. Petitioner alleged in its Petition for Review that in their contract, FII granted petitioner "a non-exclusive, non-transferrable free authority to access or use," a suite of software helpful and necessary to its operation and activities.

10. It is indeed illogical to invoke an After-Sales Service under RMC No. 44-05 when the contract between the Petitioner and FII does not pertain to a sale because the use of software was allegedly free of charge based on their agreement. Consequently, the software maintenance service fees are not considered as an After-Sales Service but definitely represent royalties.

11. The assertion that the software maintenance service fees paid by Petitioner to FII do not constitute income from sources within the Philippines is misplaced. The question of whether the income arising from labour or services is derived was sourced within or without the Philippines is irrelevant because the software maintenance service fees paid to F11 constitutes royalties from copyright rights in the software subject to 35 % [FWT] under the National Intimal Revenue Code of 1997.

11.1 Section 28 (B) (1) of the National Internal Revenue Code of 1997 provides:

"(B) Tax on Nonresident Foreign Corporation.-

In General. - Except as otherwise provided in this Code, a foreign corporation not engaged in trade or business in the Philippines shall pay a tax equal to thirty-five percent (35%) of the gross income received during each taxable year from all sources Within the Philippines, such as interest, dividends ,rents, royalties...xxx"

11.2 The above stated provision was reiterated in Section 7 (B) 2.b. of Revenue Memorandum Circular No. 44-2005 which provides:

"Section 7. MODES OF ACQUIRING SOFTWARE AND THE RELEVANT TAX TREATMENT THEREOF.

(

B. Acquisition of copyright rights

2. By an End-user

b. Directly from the foreign owner and/or licensor of the software. - A local end-user may acquire license to use software directly from the foreign licensor/owner of the software. Payments made by the end-user to the licensor/owner are royalties subject to 32 percent income tax, based on the gross amount thereof, imposed on royalties derived by a non-resident foreign corporation [Section 28 (B)(1) NIRC], which amount shall be withheld and collected by the end-user making the payments. [Section 2.57-1(I) (1), RR 2-98].

12. The contention that FII is not taxable pursuant to the RP-US Tax Treaty is untenable. Petitioner shall be subjected to the regular 35% [FWT] with regard to the royalty paid to FII for non-compliance with Revenue Memorandum Order 1-2000 which states that any availment of a tax treaty provisions must be preceded by an application for tax treaty relief with the International Tax Affairs Division (ITAD) of the Bureau of Internal Revenue.

13. Petitioner needs to secure a tax treaty relief application pursuant to RMO 1-2000 and cannot just indiscriminately rule that it is not obliged to comply with the requirement of a tax treaty relief application. Respondent cannot ascertain whether petitioner is entitled to a tax relief when no application and documentary requirements are submitted. []This is necessary in order for respondent to determine if petitioner is indeed entitled to the benefits of RP-US Tax Treaty prior to the taxable event.

14. For ease of reference, the application and procedures to be observed in processing Tax Treaty Relief Application under RMO No. 1-2000 is quoted as follows:

"III. Policies:

x x x

(2) Any availment for tax treaty relief shall be preceded by an application by filing BIR Form No. 0901 (Application for Relief from Double Taxation) with ITAD at least 15 days before the transaction i.e. payment of

dividends, royalties, etc., accompanied by supporting documents justifying the relief.

IV. Procedures:

The following procedures are to be observed in the processing of the tax treaty relief application:

1. Taxpayer

1.1 Accomplish the new BIR Form 0901 Application for Relief from Double Taxation.

1.2 File BIR Form 0901 with ITAD at least 15 days before the transaction i.e. payment of dividends, royalties, etc., with all the supposing documents justifying the relief sought.

1.3 Attach to the Withholding Tax Return Form 1734W/new computerized BIR Form 1601 (covering the final withholding taxes based the preferential tax treaty rate for income payments to non-residents), a COPY of the accomplished BIR Form 0901 duly acknowledged/received by ITAD, or when available, the approved ruling as proof of the availment of the preferential tax treaty treatment."

15. In any case, Article 5 and 8 of the RP-US Tax Treaty on Permanent Establishment as well as Business Profits is not applicable because the income constitutes royalties under Article 13 which are dealt with separately in other provisions of the tax treaty.

[15].1 Article 8 (7) of the RP-US Tax Treaty is quoted as follows:

"(7) Where business profits include items of income which are dealt with separately in other articles of this convention then the provisions of those articles shall not be affected by the provisions of this Article."

[15].2 Article 13 of the RP-US Tax Treaty reads as follows:

> "(l) Royalties derived by a resident of one of the Contracting States from sources within the other Contracting State may be taxed by both Contracting States.
>
> (2) However, the tax imposed by that other Contracting State shall not exceed-
>
> (a) In the case of the United States, 15 percent of the gross amount of the royalties, and
>
> (b) In the case of the Philippines, the least of:
>
> (i) 25 percent of the gross amount of royalties,
>
> (ii) 15 percent of the gross amount of the royalties, where the royalties are paid by a corporation registered with the Philippine Board of Investments and engaged in preferred areas of activities, and
>
> (iii) 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."

16. Furthermore, there is no violation committed by respondent in requiring compliance with RMO No. 1-2000. The said issuance is not contrary to any international treaty obligation but merely provides for reasonable policies in the application and procedures in processing tax treaty relief application.

17. It is only rational for respondent to evaluate an application and the general documents required relative to a tax treaty relief application. Respondent cannot speculate whether a corporation is entitled to a tax relief or not. It is petitioner's negligence in failing to apply and provide respondent with the necessary documents to avail the benefits of RP-US Tax Treaty prior to the taxable event.

18. The contention of petitioner that only RMO No. 72-10 requires the prior filing of tax treaty relief application in untenable because Revenue Memorandum Order No. 1-2000 in its policies provide that availment of tax treaty relief shall be

preceded by an application by filing BIR Form 1901 with the ITAD at least 15 days before the transaction.

19. Assuming arguendo that FII is a resident of a country that has an existing tax treaty with the Philippines, still the requirements and conditions prescribed under such treaty must be complied with before the royalties paid to the foreign owner can be subjected to a reduced tax rate.

20. Based on the foregoing, the finding of deficiency tax liabilities against petitioner is proper in all respects. Worthy of note, are the words of the Supreme Court in the case of Commissioner of Internal Revenue vs. Bank of Philippine Islands:

> "Tax assessments by tax examiners are presumed correct and made in good faith. The taxpayer has the duty to prove otherwise. In the absence of proof of any irregularities in the performance of duties, an assessment duly made by a Bureau of Internal Revenue examiner and approved by his superior officers will not be disturbed. All presumptions are in favour of the correctness of tax assessments."

On August 17, 2012, the parties filed their (Joint) Stipulation of Facts and Issues[28] ("JSFI"), thus, a Pre-Trial Order[29] was issued on September 10, 2012.

By virtue of the Court's October 2, 2012 Resolution[30], which states that provisions (A) 1 and 2 of petitioner's Request for Additional Admission and Stipulation[31] filed on September 20, 2012 are deemed included in the parties' JSFI[32] dated August 16, 2012, the parties admit and stipulate on the genuineness and due execution of the following documents:

1. Certification of Non-registration of Company of Fluor Intercontinental, Inc.;[33] and

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[28] *Records, Vol. I,* pp. 130-133.
[29] *Id.,* pp. 139-145.
[30] *Id.,* pp. 181-183.
[31] *Id.,* pp. 150-161, with annexes.
[32] *Id.,* pp. 130-133.
[33] *Id.,* p. 155.

2. Payment Form (BIR Form No. 0605)[34] filed *via* Electronic Filing and Payment System ("EFPS") on February 8, 2012 with Reference No. 29120000560270 0 evidencing payment of Php29,825,213.22.

On May 9, 2013, petitioner filed its Formal Offer of Evidence,[35] which was resolved by the Court on June 26, 2013,[36] to which, petitioner responded through its Motion for Reconsideration (Re: Resolution dated June 26, 2013)[37] filed on July 15, 2013, which was granted by the Court through its November 20, 2013 Resolution[38].

On February 5, 2014, petitioner filed its claim for refund or issuance of a TCC in the total amount of Php29,825,213.22 representing a portion of the deficiency FWT assessment;[39] and its Application for Tax Credits/Refunds or BIR Form No. 1914.[40]

On February 7, 2014, petitioner filed its Motion for Leave to Admit Supplemental Motion[41] with attached Supplemental Petition for Review[42], with the former granted and the latter admitted by the Court in its April 15, 2014 Resolution[43].

On the other hand, respondent filed her Formal Offer of Evidence[44] on March 10, 2014, which was resolved by the Court through its May 23, 2014 Resolution[45].

In response to the Supplemental Petition for Review, on May 13, 2014 and by registered mail, respondent filed her Supplemental Answer,[46] introducing the following Special and Affirmative Defenses:

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[34] *Records, Vol. I,* p. 156.
[35] *Id.,* pp. 232-405, with annexes.
[36] *Id.,* pp. 411-412; *Exhibits "A," "B," "C," "D," "E," "F," "G," "H," "I," "U,"* and *"U-1"* were admitted.
[37] *Id.,* pp. 413-427, with annexes.
[38] *Id.,* pp. 436-437; *Exhibits "K," "L," "M," "N," "P," "R," "S," "T," "V," "W," "X,"* and *"X-1"* were admitted.
[39] *Id., Vol. II, Exhibit "Z-1,"* pp. 759-768.
[40] *Id., Exhibit "Z,"* p. 758.
[41] *Id., Vol. I,* pp. 448-451.
[42] *Id.,* pp. 452-483, with Annexes.
[43] *Id., Vol. II,* pp. 528-529.
[44] *Id., Vol. I,* pp. 506-513.
[45] *Id., Vol. II,* p. 531; *Exhibits "R-1," "R-2," "R-3," "R-4," "R-5," "R-6," "R-7," "R-9," "R-9-A," "R-10," "R-11,"* and *"R-11-A"* were admitted.
[46] *Id.,* pp. 536-543.

SPECIAL AND AFFIRMATIVE DEFENSES

Respondent incorporates and repleads all the foregoing averments and by way of special and affirmative defenses further states:

Software maintenance service fees paid by petitioner to [FII are] considered royalties within the definition of Revenue Memorandum Circular (RMC) No. 77-2003, as further amended by RMC 44-2005

5. Revenue Memorandum Circular No. (RMC) No. 44-2005 entitled "Taxation of Payments of Software" dated September 1, 2005 explicitly provides:

> "Section 5. CHARACTERIZATION OF TRANSACTIONS - The character of payments received in a transaction involving the transfer of computer software depends on the nature of the rights that the transferee acquires under the particular arrangement regarding the use and exploitation of the program.
>
> a. Transfers of copyright rights. A transfer of software is classified as a transfer of a copyright right if, as a result of the transaction, a person acquires any one or more of the rights described below:
>
> i. The right to make copies of the software for purposes of distribution to the public by sale or other transfer of ownership, or by rental, lease or lending;
>
> ii. The right to prepare derivative computer programs based upon the copyrighted software;
>
> iii. The right to make a public performance of the software;
>
> iv. The right to publicly display the computer program[;] or
>
> v. Any other rights of the copyright owner, the exercise of which by another without his authority shall constitute infringement of said copyright.

The determination of whether a transfer of a copyright right in a software is a sale or exchange of property is made on the basis of whether, taking into account all facts and circumstances, there has been a transfer of all substantial rights in the copyright. A transaction that does not constitute a sale or chance because not all substantial rights have been transferred will be classified as a license generating royalty income.

> When only copyright rights are transferred, payments made in consideration therefore are royalties. On the other hand, when copyright ownership is transferred, payments made in consideration therefore are business income.["]

6. In relation thereto, RMC No. 77-03 dated November 18, 2003 states:

> "Definition of Royalties Includes Payments for the Use of Software:
>
> The term "royalties" as generally used means payment of any kind received as a consideration for the use of, or the right to use any copyright of literary, artistic or scientific work including cinematograph films, or films or tapes used for radio or television broadcasting, any patent, trade mark, design, or model, plan, secret formula or process, or for the use of, or the right to use, industrial, commercial or scientific equipment, or for information concerning industrial, commercial or scientific experience. The term "use" as contained herein shall include the reselling or distribution of software.
>
> Software is generally assimilated as a literary, artistic or scientific work protected by the copyright laws of various countries including the Philippines, thus, payments in consideration for the use of, or the right to use, a copyright or a copyrighted article relating to software are generally royalties.
>
> Modes of Acquiring Software and the Relevant Tax Treatment Thereof:
>
> 1. From local subsidiaries, resellers and distributors.
>
> xxx
>
> On the other hand, payments made by the local subsidiaries, resellers, or distributors to the foreign

> licensor/owner of the software as royalties are subject to thirty two percent (32%) income tax based on the gross amount thereof as that imposed on royalties derived by a nonresident foreign corporation (Section 28[B][1], NIRC), withheld and collected by the subsidiaries, resellers, or distributors making the payments (Section 2.57- 1[I][1], RR 2-98). However, if the foreign licensor/owner is a resident of a country which has an existing tax treaty with the Philippines, royalties paid thereto are subject to the reduced tax rates on royalties under the relevant tax treaty, provided the conditions prescribed therein are complied with by the licensor/owner.
>
> 2. Directly from the foreign owner and/or licensor of the software.
>
> A local end-user may acquire license to use software directly from the foreign licensor/owner of the software. Payments made by the end-user to the licensor/owner as royalties are subject to thirty two percent (32%) income tax based on the gross amount thereof as that imposed on royalties derived by a nonresident foreign corporation (Section 28[B] {1}, NIRC), withheld and collected by the end-user making the payments (Section 2.57-[1][I][1], RR 2-98). However, if the foreign licensor/owner is a resident of a country which has an existing tax treaty with the Philippines, royalties paid thereto are subject to the reduced tax rates on royalties under the relevant tax treaty, provided the conditions prescribed therein are complied with by the licensor/owner."

7. The nature of the contract executed between petitioner and FII showed that: (a) FII does not transfer all its substantial rights in the software, (b) the transactions involve only the transfer of copyright rights in the software, (c) The transaction does not constitute a sale or exchange.

8. Section 3 (b) of RMC No. 44-05 provides that the definition of royalties includes payments for the use of copyright over software, hence:

> "(b) Definition of royalties includes payments for the use of copyright over software- Software is generally assimilated as a literary, artistic or scientific work protected by the copyright laws of various countries. Thus, payments in consideration for the use of or the right to use a copyright relating to software are generally royalties."

9. The usage and access of the software is limited to the terms and conditions by FII which are stipulated in the contract. Such that, if petitioner fails to comply, it may be subject to cancellation of the contract. FII, therefore, retains full and direct control over petitioner's access and usage of the software. Hence, it loses the character of being "free" because the grant of authority is subject to various restrictions.

In a case for refund, the burden of proof is on the taxpayer to establish its right to refund, and failure to sustain the burden is fatal to the claim for refund.

10. It must be pointed out that taxes remitted to the Bureau are presumed to have been made in the regular course of business and in accordance with provisions of law.

11. Taxes are essential to government's very existence; (CIR v. Solidbank Corporation, G.R. No. 148191, November 25, 2003) hence, the dictum that "taxes are the lifeblood of the government." For this reason, the right of taxation cannot easily be surrendered, statutes granting tax exemptions are considered as a derogation of the sovereign authority. (CIR v. Fortune Tobacco Corporation, G.R. Nos. 167274-75, July 21, 2008) Since tax refunds are regarded as tax exemptions and these are to be construed strictissimi juris against the person or entity claiming the exemption. (Philippine Phospate Fertilizer Corporation vs. Commissioner of Internal Revenue G.R 141973, June 28, 2005).

12. Finally, respondent reiterates her arguments in her Answer dated May 18, 2012 as part of this Supplemental Answer.

On July 17, 2014, petitioner filed its Motion for Leave to Present Evidence in Support of Supplemental Petition for Review (With Motion to Defer Submission of Memorandum),[47] which was granted by the Court on October 30, 2014.[48]

On March 9, 2015, in open court, petitioner formally offered its additional evidence, which were all admitted by the Court.[49]

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[47] *Records, Vol. II,* pp. 547-551.
[48] *Id.,* pp. 575-576.
[49] *Id.,* pp. 719, 846-847; *Exhibits "Y," "Z," "Z-1," "AA,"* and *"AA-1"* were admitted.

On July 3, 2015, petitioner filed its Memorandum,[50] with no memorandum filed by respondent.[51]

On July 22, 2015, the Court promulgated a Resolution[52] submitting the case for Decision, hence, this Decision.

THE ISSUES[53]

1. WHETHER THE SOFTWARE MAINTENANCE SERVICE FEES PAID BY PETITIONER TO FII FOR TAXABLE YEAR 2008 CONSTITUTES ROYALTIES SUBJECT TO FWT; AND

2. WHETHER PETITIONER IS LIABLE TO PAY DEFICIENCY TAX LIABILITIES REPRESENTING FWT ON ROYALTIES FOR TAXABLE YEAR 2008, INCLUDING PENALTY AND DEFICIENCY AND DELINQUENCY INTEREST, AS PROVIDED IN SECTIONS 248 AND 249 OF THE 1997 NIRC, AS AMENDED.

THE RULING OF THE COURT

Petitioner's Arguments

Petitioner claims that it is not liable for deficiency FWT on software maintenance fees paid to FII on the ground that the same does not constitute royalty payments since there was no transfer of substantial rights in the software, it involves only the transfer of copyright rights in the software and it is not a sale or exchange; that royalty pertains to the transfer of know-how or any property of which the foreign affiliate has proprietary interest; that, under the contract, petitioner was granted free authority to access and use a suite of software helpful and necessary to its operation and activities; that petitioner is, however, required to pay its share in the software maintenance (at cost, with no markup), computed based on project hours for trouble shooting, periodic system checking and related services to ensure proper operation of the software; and that the fees

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[50] *Records, Vol. II,* pp. 861-895.
[51] *Id., Records Verification Report,* p. 896.
[52] *Id.,* p. 898.
[53] *Id., Vol. I, PTO,* p. 140.

constitute business income and not royalties; that the payments are in the nature of compensation for services rendered abroad, hence, beyond the jurisdiction of the Philippine taxing authority and cannot be taxed.

Petitioner adds that even under the assumption that the fees are Philippine sourced, it is not taxable pursuant to the RP-US Tax Treaty due to the fact that FII has no Permanent Establishment ("PE") in the Philippines; that assuming *arguendo* that they are considered as royalties, they should be taxed at the reduced rate of 10% under the RP-US Tax Treaty; and that it is entitled to a refund of the portion of the FWT paid under protest.

The Petition for Review is meritorious.

As a general rule, non-resident foreign corporations are subject to thirty-five percent (35%) income tax on its gross income, including royalties, from Philippine sources under *Section 28(B)(1) of the 1997 National Internal Revenue Code ("NIRC")*, as amended, *viz.*:

> CHAPTER IV
> Tax on Corporations
>
> SECTION 28. *Rates of Income Tax on Foreign Corporations.* –
>
> xxx xxx xxx
>
> (B) *Tax on Nonresident Foreign Corporation.* –
>
> (1) *In General.* – <u>Except as otherwise provided in this Code, a foreign corporation not engaged in trade or business in the Philippines shall pay a tax equal to thirty-five percent (35%) of the gross income received during each taxable year from all sources within the Philippines, such as</u> interests, dividends, rents, <u>royalties,</u> salaries, premiums (except reinsurance premiums), annuities, emoluments or other fixed or determinable annual, periodic or casual gains, profits and income, and capital gains, except capital gains subject to tax under subparagraph 5(c): *Provided,* That effective January 1, 2009, the rate of income tax shall be thirty percent (30%).

As above-stated, a non-resident foreign corporation shall be exempt from income tax if so provided by the *1997 NIRC*, as amended.

Reference to *Section 32(B)(5) of the 1997 NIRC,* as amended, will reveal that the *1997 NIRC* recognizes the Philippines' treaty obligations granting income tax exemptions, to wit:

CHAPTER VI
Computation of Gross Income

SECTION 32. *Gross Income.* —

xxx xxx xxx

(B) *Exclusions from Gross Income.* — The following items shall not be included in gross income and shall be exempt from taxation under this Title:

xxx xxx xxx

(5) *Income Exempt under Treaty.* — Income of any kind, to the extent required by any treaty obligation binding upon the Government of the Philippines.

One such treaty is the *Republic of the Philippines ("RP") - United States of America ("US") Tax Treaty*[54] ("Tax Treaty"), which took effect on January 1, 1983, the salient provisions thereof affecting royalties are the following:

ARTICLE 4
SOURCE OF INCOME

xxx xxx xxx

(3) <u>Royalties for the use of, or the right to use, property or rights shall be treated as income from sources within a Contracting State only to the extent that such royalties are for the use of, or the right to use, such property or rights within that Contracting State.</u> Notwithstanding the preceding sentence, if such royalty is paid with respect to a liability to pay the royalty that was incurred in connection with a permanent establishment which bears such royalty, then such royalty shall be deemed to be from sources within the State (whether or not a Contracting State) in which the permanent establishment is situated.

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[54] Convention Between the Government of the Republic of the Philippines and the Government of the United States of America with Respect to Taxes on Income, signed on October 1, 1976; noteworthy is the fact that the 1997 NIRC became effective only on January 1, 1998.

xxx xxx xxx

(6) Notwithstanding paragraphs (1) through (4), business profits which are attributable to a permanent establishment which the recipient, a resident of one of the Contracting States, has in the other Contracting State shall be treated as income from sources within that other Contracting State.

xxx xxx xxx

(8) The source of any item of income to which paragraphs (1) through (7) are not applicable shall be determined by each of the Contracting States in accordance with its own law. Notwithstanding the preceding sentence, if the source of any item of income under the laws of one Contracting State is different from the source of such item of income under the laws of the other Contracting State or if the source of such income is not readily determinable under the laws of one of the Contracting States, the competent authorities of the Contracting States may, in order to prevent double taxation or further any other purpose of this Convention, establish a common source of the item of income for the purposes of this Convention.

xxx xxx xxx

ARTICLE 13
ROYALTIES

(1) Royalties derived by a resident of one of the Contracting States from sources within the other Contracting State may be taxed by both Contracting States.

(2) However, the tax imposed by that other Contracting State shall not exceed –

(a) In the case of the United States, 15 percent of the gross amount of the royalties, and

(b) In the case of the Philippines, the least of:
- (i) 25 percent of the gross amount of the royalties,
- (ii) 15 percent of the gross amount of the royalties, where the royalties are paid by a corporation registered with the Philippine Board of Investments and engaged in preferred areas of activities, and
- (iii) 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.

(3) The term "royalties" as used in this Article means payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work, including cinematographic films or films or tapes used for radio or television broadcasting, any patent, trade mark, design or model, plan, secret formula or process, or other like right of property, or for information concerning industrial, commercial or scientific experience. The term "royalties" also includes gains derived from the sale, exchange or other disposition of any such right or property which are contingent on the productivity, use, or disposition thereof.

xxx xxx xxx

(4) The provisions of paragraphs (1) and (2) shall not apply if the recipient of the royalties, being a resident of a Contracting State, carries on business in the other Contracting State in which the royalties arise, through a permanent establishment situated therein, or performs in that other State professional services from a fixed base situated therein, and the right or property in respect of which the royalties are paid is effectively connected with such permanent establishment or fixed base. In such a case, the provisions of Article 8 (Business Profits) or Article 15 (Independent Personal Services), as the case may be, shall apply.

From the above, it is imperative for the Court to determine the following:

1. Whether petitioner and FII fall under the definition of "residents" under the Tax Treaty;

2. Whether FII has a PE in the Philippines;

3. Whether the nature of the payments made by petitioner to FII fall under the definition of "royalties" under the Tax Treaty; and

4. If applicable:

   a. Whether the refund was timely filed;
   b. Whether the assessment should be upheld; and

c. The amount refundable to petitioner.

Petitioner and FII fall under the definitions of "resident of the Philippines" and "resident of the US," respectively.

Article 3 of the Tax Treaty on Fiscal Residence sheds light on the first question:

ARTICLE 3
FISCAL RESIDENCE

(1) In this Convention:

(a) The term "resident of the Philippines" means:

(i) A Philippine corporation, and
(ii) xxx

(b) The term "resident of the United States" means:

(i) A United States corporation, and
(ii) xxx

It is undisputed and was so provided in the JSFI that petitioner is a domestic corporation duly organized and existing under and by virtue of the laws of the Republic of the Philippines.[55] Hence, it is a resident of the Philippines by the definition found in *Article 3(1)(a)(i) of the Tax Treaty*.

As to FII, records reveal that it is indeed a resident of the United States within the meaning provided in *3(1)(b)(i) of the Tax Treaty*, through the following documents:

1. Duly consularized[56] Certificate of Amendment of Articles of Incorporation of Fluor Daniel Intercontinental, Inc., endorsed and filed with the Office of the Secretary of State of the State of California, dated February 14, 2002, wherein the name if

[55] *Records, Vol. I, JSFI, par. 1,* p. 130.
[56] *Id., Exhibit "R,"* pp. 359-363; as required under *Section 24* in relation to *Section 19(A), Rule 132(B), Revised Rules of Evidence.*

the corporation was changed to "Fluor Intercontinental, Inc." and wherein it is stated that the corporation is a California corporation;[57] and

2. Certification of Non-Registration of Company issued by the Philippine Securities and Exchange Commission ("SEC") on July 17, 2012, which certifies that its records do not show the registration of "Fluor Intercontinental, Inc." as a corporation or as a partnership.[58]

FII has no Permanent Establishment in the Philippines.

Next, the Court shall determine if FII has a PE in the Philippines. The pertinent provisions of the *Tax Treaty* are the following:

ARTICLE 5
PERMANENT ESTABLISHMENT

(1) For the purposes of this Convention, the term "permanent establishment" means a fixed place of business through which a resident of one of the Contracting States engages in a trade or business.

(2) The term "fixed base of business" includes but is not limited to:

(a) A seat of management;

(b) A branch;

(c) An office;

(d) A store or other sales outlet;

(e) A factory;

(f) A workshop;

(g) A warehouse;

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[57] *Records, Vol. I, Exhibit "R,"* p. 364.
[58] *Id., Exhibit "S,"* p. 377.

(h) A mine, quarry, or other place of extraction of natural resource;

(i) A building side or construction or assembly project or supervisory activities in connection therewith, provided such site, protect or activity continues for a period of more than 183 days; and

(j) The furnishing of services, including consultancy services, by a resident of one of the Contracting States through employees or other personnel, provided activities of that nature continue (for the same or a connected project) within the other Contracting State for a period or periods aggregating more than 183 days.

The Court finds no evidence to prove that FII has established a PE in the Philippines. More importantly, the following support and demonstrate that there is no such PE:

1. Duly consularized Certificate of Amendment of Articles of Incorporation[59], which provides that FII is a California corporation;

2. Certification of Non-Registration of Company issued by SEC[60], which states that FII is not registered as a corporation or as a partnership;

3. Official Receipts that provide that the maintenance services were performed in the United States;[61]

4. Mr. Ramon M. Villaflores' Judicial Affidavit ("JA") and Revised Supplemental JA, which stipulate the following:

a. That FII does not maintain an office in the Philippines;[62] and

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[59] *Records, Vol. I, Exhibit "R,"* p. 364; consularized on July 18, 2012, pp. 359-363.
[60] *Id., Exhibit "S,"* p. 377.
[61] *Id., Exhibits "K," "L," "M,"* and *"N."*
[62] *Id., Exhibit "Y,"* p. 422.

b. That, in the course of the performance of maintenance services, FII did not provide or second personnel to petitioner;[63]

The payments made by petitioner to FII were all made under a service contract pursuant to the Licensing Contract.

Having determined that there was no PE on the part of FII, the Court now looks into the nature of the payments made by petitioner.

On January 1, 2004, petitioner and FII entered into a Licensing Contract[64] whereby the latter, as licensor and user of the suite of software, granted the former a non-exclusive, non-transferrable free authority to access and use the said suite, a necessary tool in the performance of its activities.[65] It is, likewise, stipulated therein that access and usage are free but petitioner is required to pay a maintenance service fee, to FII as an independent contractor, for every home office and field staff project hour.[66] It further provides that services are rendered outside the Philippines; that petitioner shall not make use of the software for time-sharing or otherwise allow third parties to use the same without FII's approval; that petitioner can make copies of the software for distribution to its employees to the extent necessary for petitioner's use and access but not to third parties; and that petitioner is not allowed to decompile, disassemble, reverse-engineer, modify, adapt, or create derivative works from, the software.

Pursuant to the Licensing Contract for the year 2008, petitioner was charged by FII the following amounts in United States Dollars ("USD") with the heading reading "CHARGES FOR USAGE OF ENGINEERING SOFTWARE SUITE" and with the description "CHARGES / FEES FOR SOFTWARE MAINTENANCE SERVICES RENDERED IN THE U.S...," *viz.*:

QUARTER	EXHIBIT	OR NO.	OR DATE	AMOUNT
First	"K"[67]	2008-Phil-01	March 29, 2008	809,734.00

[63] *Records, Vol. I, Exhibit "Y,"* p. 423.
[64] *Id., Licensing Contract, Exhibit "T,"* pp. 378-385, with Annexes.
[65] *Id., Licensing Contract, Exhibit "T,"* p. 378.
[66] *Id., Licensing Contract, Exhibit "T,"* p. 379.
[67] *Id.*, p. 316.

Second	"L"[68]	2008-Phil-02	June 27, 2008	773,021.00
Third	"M"[69]	2008-Phil-03	September 26, 2008	628,310.00
Fourth	"N"[70]	2008-Phil-04	December 31, 2008	580,795.00
TOTAL				**2,791,860.00**

The above total amount was reflected in petitioner's Audited Financial Statements ("AFS")[71], which states that FII provides software maintenance services to petitioner; that the cost amounted to USD2,791,860.00 in 2008; and that it is included in "Business support services" account under Cost of Services.[72]

It is clear from the plain reading of the contract that the use of the suite of software is free and that petitioner will only pay FII a fee to shoulder its share in the maintenance of the software.

Petitioner and FII's actions after entering into the contract, specifically in 2008, illustrate their previous agreement (*i.e.* Licensing Contract), in the following manner:

1. FII charged petitioner only for "software maintenance services;" and

2. Petitioner reflected payments in the AFS as "business support services."

Reference to the previously-quoted provisions on royalties in the *Tax Treaty* leads to the definition of "royalties" as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work, or for information concerning industrial, commercial or scientific experience.

Since the above definition is broad, the *Commentaries on the 2010 Economic Co-operation and Development ("OECD") Model Tax Convention on Income and on Capital* ("OECD Commentary") shall give light on nature of the payments made in relation to the concepts of a "know-how" contract *vis-à-vis* a service contract, to wit:[73]

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[68] *Records, Vol. I,* p. 317.
[69] *Id.,* p. 318.
[70] *Id.,* p. 319.
[71] *Id., AFS, Exhibit "P,"* pp. 320-358.
[72] *Id., AFS, Exhibit "P," Notes 10 (a) and 11,* pp. 346-347.
[73] OECD Model Tax Convention on Income and Capital, Condensed Version, July 2010, pp. 222-226; emphases ours.

**COMMENTARY ON ARTICLE 12
CONCERNING THE TAXATION OF ROYALTIES**

II. Commentary on the provisions of the Article

xxx xxx xxx

Paragraph 2

8. Paragraph 2 contains a definition of the term "royalties". These relate, in general, to rights or property constituting the different forms of literary and artistic property, the elements of intellectual property specified in the text and information concerning industrial, commercial or scientific experience. The definition applies to payments for the use of, or the entitlement to use, rights of the kind mentioned, whether or not they have been, or are required to be, registered in a public register. The definition covers both payments made under a license and compensation which a person would be obliged to pay for fraudulently copying or infringing the right.

xxx xxx xxx

8.3 The word "payment", used in the definition, has a very wide meaning since the concept of payment means the fulfilment of the obligation to put funds at the disposal of the creditor in the manner required by contract or by custom.

8.4 As a guide, certain explanations are given below in order to define the scope of Article 12 in relation to that of other Articles of the Convention, as regards, in particular, the provision of information.

xxx xxx xxx

11. In classifying as royalties payments received as consideration for information concerning industrial, commercial or scientific experience, paragraph 2 is referring to the concept of "know-how". Various specialist bodies and authors have formulated definitions of know-how. The words "payments ... for information concerning industrial, commercial or scientific experience" are used in the context of the transfer of certain information that has not been patented and does not generally fall within other categories of intellectual property rights. It generally corresponds to undivulged information of an industrial, commercial or

scientific nature arising from previous experience, which has practical application in the operation of an enterprise and from the disclosure of which an economic benefit can be derived. Since the definition relates to information concerning previous experience, the Article does not apply to payments for new information obtained as a result of performing services at the request of the payer.

11.1 In the know-how contract, one of the parties agrees to impart to the other, so that he can use them for his own account, his special knowledge and experience which remain unrevealed to the public. It is recognised that the grantor is not required to play any part himself in the application of the formulas granted to the licensee and that he does not guarantee the result thereof.

11.2 This type of contract thus differs from contracts for the provision of services, in which one of the parties undertakes to use the customary skills of his calling to execute work himself for the other party. Payments made under the latter contracts generally fall under Article 7.

11.3 The need to distinguish these two types of payments, *i.e.* payments for the supply of know-how and payments for the provision of services, sometimes gives rise to practical difficulties. The following criteria are relevant for the purpose of making that distinction:

– Contracts for the supply of know-how concern information of the kind described in paragraph 11 that already exists or concern the supply of that type of information after its development or creation and include specific provisions concerning the confidentiality of that information.

– In the case of contracts for the provision of services, the supplier undertakes to perform services which may require the use, by that supplier, of special knowledge, skill and expertise but not the transfer of such special knowledge, skill or expertise to the other party.

– In most cases involving the supply of know-how, there would generally be very little more which needs to be done by the supplier under the contract other than to supply existing information or reproduce existing material. On the other hand, a contract for the performance of services would, in the majority of cases, involve a very much greater level of expenditure by the supplier in order to perform his contractual obligations. For instance, the supplier, depending on the nature of the services to be rendered, may have to incur salaries and wages for employees engaged in researching, designing, testing, drawing and other associated activities or payments to sub-contractors for the performance of similar services.

Based on the foregoing, it can be gathered that the present Licensing Contract deals with both "know-how" contract (for the use of the suite of software) and service contract (for maintenance of the software). The Court will not dwell on the "know-how" contract since FII did not receive any income therefor. As to the service contract, the *OECD Commentary* refers to *Article 8 (Business Profits)*[74] of the *RP-US Tax Treaty, viz.*:

ARTICLE 8
BUSINESS PROFITS

(1) Business profits of a resident of one of the Contracting States shall be taxable only in that State unless the resident has a permanent establishment in the other Contracting State. If the resident has a permanent establishment in that other Contracting State, tax may be imposed by that other Contracting State on the business profits of the resident but only on so much of them as are attributable to the permanent establishment.

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(6) The term "business profits" means income derived from any trade or business whether carried on by an individual, corporation or any other person, or group of persons, including the rental of tangible personal (movable) property.

(7) Where business profits include items of income which are dealt with separately in other articles of this Convention, then the provisions of those articles shall not be affected by the provisions of this Article.

It can be gathered from the above that business profits of FII shall be taxable only in the US unless it has a PE in the Philippines. Considering the fact that the Court has already concluded that FII has

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[74] instead of *Article 7 (Income from Real Property).*

no PE in the Philippines, FII's income from the maintenance service fees is, therefore, exempt from income tax.

The above statement is strengthened by the provisions of the *1997 NIRC*, as amended, itself, as follows:

TITLE II
Tax on Income

CHAPTER I
Definitions

SECTION 22. *Definitions.* — When used in this Title:

xxx xxx xxx

(D) The term 'foreign,' when applied to a corporation, means a corporation which is not domestic.

xxx xxx xxx

CHAPTER II
General Principles

SECTION 23. *General Principles of Income Taxation in the Philippines.* — Except when otherwise provided in this Code:

xxx xxx xxx

(F) <u>A foreign corporation, whether engaged or not in trade or business in the Philippines, is taxable only on income derived from sources within the Philippines.</u>

Having established that the services were rendered in the US, or outside the Philippines, the Court concludes that the payments made by petitioner to FII for service maintenance fees are beyond the taxing jurisdiction of the Philippine taxing authority or the BIR. Therefore, these are exempt from income tax in the form of FWT.

As to the issue of prior application for tax treaty relief, the Supreme Court ruled on this in the landmark case of *Deutsche Bank AG Manila Branch v. Commissioner of Internal Revenue*[75], wherein the Highest Tribunal explained that laws and issuances must ensure that

[75] G.R. No. 188550, August 19, 2013, 704 SCRA 216.

the reliefs granted under tax treaties are accorded to the parties entitled thereto; and that the BIR must not impose additional requirements that would negate the availment of the reliefs provided for under international agreements. Hence, if no such prior application is required by the treaty, there is no basis to demand the same by administrative issuance.

The administrative and judicial claims for refund were timely filed.

Having determined that petitioner is not liable for FWT paid under protest on the software maintenance services and before looking into whether petitioner is entitled to a refund thereof, the Court shall first resolve whether petitioner filed its administrative and judicial claims within the period provided by law.

The pertinent provisions are *Sections 204(C) and 229 of the 1997 NIRC*, as amended, which provide as follows:

> *Sec. 204. Authority of the Commissioner to Compromise, Abate, and Refund or Credit Taxes. – The Commissioner may –*
>
> xxx xxx xxx
>
> (C) Credit or refund taxes erroneously or illegally received or penalties imposed without authority, refund the value of internal revenue stamps when they are returned in good condition by the purchaser, and, in his discretion, redeem or change unused stamps that have been rendered unfit for use and refund their value upon proof of destruction. <u>No credit or refund of taxes or penalties shall be allowed unless the taxpayer files in writing with the Commissioner a claim for credit or refund within two (2) years after the payment of the tax or penalty:</u> *Provided,* however, That a return filed showing an overpayment shall be considered as a written claim for credit or refund.
>
> xxx xxx xxx
>
> *SEC. 229. Recovery of Tax Erroneously or Illegally Collected.* - No suit or proceeding shall be maintained in any court for the recovery of any national internal revenue tax hereafter alleged to have been erroneously or illegally assessed or collected, or of

> any penalty claimed to have been collected without authority, of any sum alleged to have been excessively or in any manner wrongfully collected without authority, or of any sum alleged to have been excessively or in any manner wrongfully collected, until a claim for refund or credit has been duly filed with the Commissioner; but such suit or proceeding may be maintained, whether or not such tax, penalty, or sum has been paid under protest or duress.
>
> In any case, <u>no such suit or proceeding shall be filed after the expiration of two (2) years from the date of payment of the tax or penalty regardless of any supervening cause that may arise after payment</u>: Provided, however, That the Commissioner may, even without a written claim therefor, refund or credit any tax, where on the face of the return upon which payment was made, such payment appears clearly to have been erroneously paid.

It is clear, therefore, that a taxpayer who claims for refund under *Section 229 of the 1997 NIRC*, as amended, on the ground of erroneous payment must be able to prove that it has paid the tax and such payment was erroneous.[76] It is also clear that the taxpayer must prove that a written claim for the refund or credit thereof was duly filed with the CIR, and that the suit or proceeding was instituted within two (2) years from the date of payment of the tax or penalty.

Petitioner submitted Payment Form or BIR Form No. 0605[77] filed on February 8, 2012, together with EFPS Confirmation Receipt[78] to prove that the payment of the above-mentioned tax and interest were actually collected by the respondent on February 10, 2012 through petitioner's bank. Hence, the claims should be filed two (2) years thereafter, or by February 10, 2014.

On February 5, 2014, petitioner filed its administrative claim for refund[79] and on February 7, 2014, it filed the Supplemental Petition for Review[80] which finally prayed for the refund of the FWT paid under protest. Given the foregoing dates, the present claim for refund was filed within the two (2)-year prescriptive period.

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[76] *Commissioner of Internal Revenue v. Ericsson Telecommunications, Inc.*, CTA *EB* Case No. 947, September 12, 2013.
[77] *Records, Vol. I, Exhibit "G,"* p. 293-294.
[78] *Id., Exhibit "G,"* p. 297.
[79] *Id., Vol. 2, Exhibit "Z,"* p. 758; *Exhibit "Z-1,"* pp. 759-768.
[80] *Id., Vol. I,* pp. 452-483, with annexes.

Petitioner is entitled to the refund claimed in the total amount of Php29,825,213.

The parties already admitted and stipulated on the genuiness and due execution of petitioner's Payment Form (BIR Form No. 0605)[81] filed *via* EFPS on February 8, 2012 with Reference No. 291200005602700 evidencing payment of Php29,825,213.22.[82]

On top of this, petitioner presented TAF[83], proving payment under protest the said amount of Php29,825,213.22, representing fifteen percent (15%)[84] FWT and interest, as shown below:

Basic FWT	P	18,444,938.71
Interest		11,380,274.51
Total	**P**	**29,825,213.22**

As previously stated, aside from the filing of the refund claim within the prescriptive period, *Section 229 of the 1997 NIRC,* as amended, requires the taxpayer to prove that the tax has been erroneously or illegally collected, or that the penalty has been collected without authority, and/or that any sum has been excessively or in any manner wrongfully collected.[85]

Having extensively discussed the reasons why the FWT on the service maintenance fees should not have been collected and that the FWT at the rate of 15% was indeed paid by petitioner under protest, petitioner is entitled to the refund claimed.

The remaining deficiency FWT assessment on royalties has no basis.

[81] *Records, Vol. I,* p. 156.
[82] *Id., October 2, 2012 Resolution,* pp. 181-183.
[83] *Id., Exhibit "D,"* p. 281.
[84] *Id., Exhibits "I"* to *"I-1,"* with annexes, pp. 303-315.
[85] *Commissioner of Internal Revenue v. Ericsson Telecommunications, Inc.,* CTA *EB* Case No. 947, September 12, 2013.

Based on the records, the deficiency FWT assessment was computed in the following manner:

Software Maintenance Service fee (Royalties) paid to [FII]	P	122,966,285.05
WF Rate		35%
Total	P	43,038,190.32
Less: Remittance per Return		-
Deficiency WF	P	43,038,190.32
Add: Interest		26,553,973.86
TOTAL DEFICIENCY WITHHOLDING TAX	**P**	**69,592,164.18**

Given the payment of petitioner in the amount of Php29,825,213.22, the remaining balance of Php39,766,950.96 was demanded by respondent in the FDDA[86].

As already discussed, the software maintenance fees paid to FII are not subject to FWT, hence, the remaining assessment cannot be sustained.

WHEREFORE, the instant Petition for Review is hereby **GRANTED**.

The Final Decision on Disputed Assessment dated February 13, 2012 and the relating assessment for Final Withholding Tax against petitioner Fluor Daniel Inc. - Philippines in the total amount of **SIXTY-NINE MILLION FIVE HUNDRED NINETY-TWO THOUSAND ONE HUNDRED SIXTY-FOUR AND 18/100 PESOS (Php69,592,164.18)** is hereby **CANCELLED** and **SET ASIDE**.

Accordingly, respondent is hereby **ORDERED TO REFUND OR TO ISSUE A TAX CREDIT CERTIFICATE** in favor of petitioner in the amount of **TWENTY-NINE MILLION EIGHT HUNDRED TWENTY-FIVE THOUSAND TWO HUNDRED THIRTEEN AND 22/100 PESOS (Php29,825,213.22)** representing Final Withholding Tax on Royalties paid under protest.

SO ORDERED.

LOVELL R. BAUTISTA
Associate Justice

[86] *Records, Vol. I, Exhibit "C,"* pp. 278-280.

WE CONCUR:

ESPERANZA R. FABON-VICTORINO
Associate Justice

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

ATTESTATION

I attest that the conclusions in the above Decision were reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

LOVELL R. BAUTISTA
Associate Justice
Chairperson

CERTIFICATION

Pursuant to *Section 13 of Article VIII of the Constitution* and the Division Chairperson's Attestation, it is hereby certified that the conclusions in the above Decision were reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

ROMAN G. DEL ROSARIO
Presiding Justice