REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

FIRST DIVISION

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AMERICAN POWER CONVERSION (PHILIPPINES), INC.,
Petitioner,

C.T.A. CASE NO. 6817

Members:

- versus -

ACOSTA, *Chairperson*
BAUTISTA, and
CASANOVA, *JJ.*

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:
FEB 22 2007 9:15 PM

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DECISION

CASANOVA, C., J.:

This is a Petition for Review seeking the refund of the 20% and 7½% final withholding tax on interests earned by petitioner on its local currency bank deposits and yield and on its deposits under the expanded foreign currency deposit system in the amounts of **ONE HUNDRED ELEVEN THOUSAND SEVEN HUNDRED NINETY TWO AND 07/100 PESOS (P111,792.07)** and **THIRTY NINE THOUSAND NINE HUNDRED THREE AND 57/100 US DOLLARS (US$ 39,903.57),** respectively, alleged to be erroneously withheld and remitted to the respondent by Citibank, BPI and RCBC for the period covering the first quarter of 2001 to July 2003.

Petitioner is a domestic corporation duly registered with the Securities and Exchange Commission ("SEC"), with office address at the Cavite Ecozone, Rosario, Cavite. It was organized to engage in, operate, conduct and maintain the business of manufacturing, processing, importing, exporting, buying, selling and/or dealing in, on a wholesale basis, electronic equipment, power goods of similar nature and their accessories of whatever nature and character, and any and all equipment, materials, supplies used or employed in or related to the manufacture of finished products.[1]

Respondent is the Commissioner of Internal Revenue ("CIR"), duly appointed to perform the duties of his office, including, *inter alia*, the power to decide claims for refund of erroneously paid internal revenue taxes, subject to the exclusive appellate jurisdiction of this Court, pursuant to Section 4 of the 1997 Tax Code.[2]

Petitioner is a Philippine Economic Zone Authority ("PEZA")-registered enterprise, as shown by its PEZA Certificate of Registration No. 96-060 dated May 15, 1996.[3] As such, petitioner was initially entitled to an Income Tax Holiday ("ITH") of four (4) years from the start of its commercial operations as a non-pioneer enterprise. However, as petitioner's status was converted to a "pioneer enterprise", a six (6)-year income tax holiday under PEZA Board Resolution No. 01-150[4] was granted. Subsequently, a one (1) year extension was further approved under PEZA Notice of ITH Extension Approval No. 02-008 dated January 31, 2002.[5]

For the period covering the first quarter of the taxable year 2001 to July 2003, petitioner allegedly earned interest income from its Philippine peso and foreign currency bank/time deposits with Citibank, Bank of the Philippine Islands ("BPI") and Rizal Commercial Banking Corporation ("RCBC") in the total amount of Php558,960.54 and

[1] Par. 1(a), Joint Stipulation of Facts and Issues.
[2] Par. 1(b), Joint Stipulation of Facts and Issues.
[3] Exhibit "B"; Par. 1(c), Joint Stipulation of Facts and Issues.
[4] Exhibit "C"; per Board Meeting held on April 26, 2001.
[5] Exhibit "E".

US$532,047.44, respectively.[6] For these interest income earned, Citibank, BPI and RCBC withheld from petitioner and remitted to the Bureau of Internal Revenue (BIR) the amounts of Php111,792.07 and US$39,903.57 representing the 20% and 7½% final withholding taxes, respectively.

On the belief that it is not liable to pay the said final taxes of 20% and 7½% pursuant to the income tax holiday incentive granted to business establishments operating within the ECOZONES pursuant to the Special Economic Zone Act of 1995[7] ("PEZA Law"), petitioner then filed on October 6, 2003, an administrative claim for refund with the BIR of taxes alleged to be erroneously withheld and remitted by the aforementioned banks to the BIR.[8]

Having received no reply from the respondent and before it could be barred by prescription, petitioner filed the instant Petition for Review with this Court on November 20, 2003.

On January 27, 2004, respondent filed his Answer interposing the following Special and Affirmative Defenses:

4. He reiterates and repleads the preceding paragraphs of this answer as part of his Special and Affirmative Defenses;

5. Petitioner's alleged claim for refund is subject to administrative investigation/examination by the respondent;

6. To support its claim, it is imperative for petitioner to prove the following, viz:

    a. The PEZA registration and status of registration of petitioner from 2001-2003;
    b. Proof of taxes on interest income withheld and remitted to the BIR by the depositary bank;
    c. That petitioner's administrative and judicial claims for tax credit or refund of the final taxes on interest income were filed within two (2) years from the date of payment of the tax in accordance with Section 229 of the Tax Code, as amended.

[6] See Annex "C", Petition for Review, Records, p. 15.
[7] Republic Act No. 7916.
[8] Exhibit "K".

7. Furthermore, in an action 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/credit. This is so because exemptions from taxation are highly disfavored in law, and he who claims exemption must be able to justify his claim by the clearest grant of organic or statutory law. An exemption from the common burden cannot be permitted to exist upon vague implications (Asiatic Petroleum Co. (P.I.) vs. Llanes, 49 Phil 466 cited in Collector of Internal Revenue v. Manila Jockey Club, Inc., 98 Phil. 670); and

8. Claims for refund are construed strictly against the claimant for the same partake (of) the nature of exemption from taxation.

On August 4, 2006, this case was deemed submitted for Decision sans the Memorandum of respondent

The parties have jointly stipulated that only the following issues are to be resolved by this Court:

1. Whether or not the petitioner's administrative and judicial claim for refund were filed within two (2) years from the date of payment of the tax in accordance with Section 229 of the 1997 Tax Code; and

2. Whether or not petitioner, through its depository banks, erroneously paid and remitted to the Bureau of Internal Revenue (BIR) the 20% and 7½% final withholding taxes on interest earned from local and foreign currency deposits, respectively.

As regards the first issue, petitioner relies on the provision of Section 229 of the National Internal Revenue Code of 1997, which is quoted hereunder for expediency:

> **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, 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, 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: *Provided, however*, That the Commissioner may, even without a written claim therefore, 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.

Petitioner asserts that its administrative claim for refund filed on October 6, 2003[9] and this instant judicial claim filed on November 20, 2003 were both filed within the two (2)-year prescriptive period allowed by law.

This Court partly agrees.

Petitioner's claim involved alleged erroneous payments of the 20% and 7½% final taxes on its interest income derived from its local and foreign currency bank deposits or yields covering the taxable years starting the first quarter of 2001 to July 2003. Based on the above law, its claim for refund of erroneously or illegally collected taxes should be filed within two (2) years from its date of payment or remittance to the respondent. Further, the return for the subject final withholding taxes should be filed and payment made within twenty-five (25) days from the close of each quarter.[10]

In the case at bench, petitioner, through its withholding agents, is required to file its final withholding tax returns and pay the taxes due thereon for the first, second and third quarters of 2001 on April 25, 2001; July 25, 2001 and October 25, 2001 respectively. Counting the two (2)-year prescriptive period from these dates, petitioner had until April 25, 2003; July 25, 2003 and October 27, 2003 within which to file its claim for refund for these quarters. Verily, petitioner's claim for refund of erroneously paid final taxes on its interest income for the first three (3) quarters of the taxable year 2001 has already prescribed. It has been admitted that petitioner filed its administrative claim for refund on October 3, 2003 and the judicial claim on November 20, 2003. Clearly, beyond the two (2)-year prescriptive period with respect to the first three (3) quarters of 2001.

As regards the second issue, petitioner alleges that it has paid and remitted to the BIR 20% and 7½% final withholding taxes on interests earned from local and foreign

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[9] Exhibit "K".

[10] SEC. 2.58. Returns and Payment of Taxes Withheld at Source.

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(c) The return for final withholding taxes on interest from any currency bank deposit and yield or any other monetary benefit from deposit substitutes and from trust funds and similar arrangements shall be filed and the payment made within twenty-five (25) days from the close of each quarter.

currency deposits as evidenced by the following documents:

1. BPI certification of taxes withheld from March 2001 to June 2003 *(Exhibit "F");*

2. BPI Bank Statements *(Exhibits "F-1" to "F-10");*

3. Certificates of Final Tax Withheld at Source issued by BPI-Rosario Branch for the year 2001 to 2003;

4. Citibank Certification of taxes withheld under its peso and dollar current account from 2001 to 2003 *(Exhibit "G");*

5. Citibank Bank Statements for petitioner's peso current account *(Exhibits "G-1" to "G-11");*

6. Certificates of Final Income Tax Withheld at Source on petitioner's interest income from its peso current account issued by Citibank N.A. for the years 2001 to 2003 *(Exhibits "G-12" to "G-14");*

7. Citibank Bank Statements for petitioner's dollar current account *(Exhibits "H", "H-1" to "H-9");*

8. Certificates of Final Income Tax Withheld at Source on petitioner's interest income from its dollar current account issued by Citibank N.A. for the years 2001 to 2003 *(Exhibits "H-10" to "H-12");*

9. Citibank Confirmation Certification of interest earned and taxes withheld on petitioner's multi money time deposits from 2001 to 2003 *(Exhibit "I");*

10. Citibank Client Confirmations on the roll-over of petitioner's multi money time deposits *(Exhibits "I-1" to "I-4");*

11. Certificates of Final Income Tax Withheld at Source on petitioner's interest income from its multi money time deposit issued by Citibank N.A. for the years 2001 to 2003 *(Exhibits "I-5" to "I-7");*

12. RCBC certification on taxes withheld on interest earned on deposits of Petitioner from March 2001 to June 2003 *(Exhibit "J");*

13. RCBC Account Passbooks of petitioner *(Exhibits "J-1," "J-2," "J-3," "J-4," "J-5," "J-6," "J-7," "J-8," "J-9," and "J-10,");*

14. Certificates of Income Tax Withheld from March 2001 to June 2003 *(Exhibits "J-1-a," "J-2-a," "J-3-a," "J-4-a," "J-5-a," "J-6-a," "J-6-a," "J-7-a," "J-8-a," "J-9-a," and "J-10-a");* and

15. Annual Information Returns of income taxes withheld on interest earned by petitioner issued by RCBC for 2001 to 2003 *(Exhibits "J-11" to "J-13").*

A review of the above documents reveals that indeed petitioner, through its depository banks, Citibank, BPI and RCBC, has paid and remitted the subject final withholding taxes. The question now is whether the payment and remittance of the same were erroneous.

Petitioner maintains that its interest income for the period covering the first quarter of 2001 to July 2003 is not subject to the final withholding taxes of 20% and 7½% as it is exempt from the payment of all kinds of income taxes which may be levied by the National Government pursuant to its entitlement to an income tax holiday under Article 39(a)(1) of the PEZA Law. Petitioner submits that under its PEZA registration[11] on a pioneer status, it enjoys a six (6)-year income tax holiday from the start of its commercial operations, or from August 1, 1996, until July 31, 2003, after which it shall be subject to the 5% preferential tax in lieu of all national and local taxes.

This Court disagrees.

It is undisputed that Section 23 of Republic Act No. 7916, otherwise known as the Special Economic Zone Act of 1995 ("PEZA Law") provides that business establishments operating within the ECOZONES shall be entitled to the fiscal incentives as provided under Presidential Decree No. 66, the Law creating the Export Processing Zone Authority, or those provided under Book VI of Executive Order No. 226, otherwise known as the Omnibus Investments Code. Pursuant to petitioner's registration as a PEZA establishment and its grant of a pioneer status, petitioner was entitled to a six-year Income Tax Holiday ("ITH") incentive commencing from the date of its start of business operations, or on August 1, 1996.[12]

In a nutshell, the ITH incentive clearly allows the petitioner an exemption from the payment of all taxes which may be levied by the National Government for a period of six (6) years from the start of its business operations. Thus, when petitioner started on August 1,

[11] Exhibit "B".
[12] Exhibit "C".

1996, it had until July 31, 2003 within which to enjoy such incentive, provided that it complies with the conditions as set forth by the PEZA Law.

However, this incentive does not necessarily include every and all kinds of income which the petitioner may receive during the period of availment.

Income gained or received by a taxpayer must be those income effectively connected with the conduct of its trade or business. An effectively connected income may be interpreted to mean as those income derived from the business activity in which the corporation is engaged in. These are shown when the taxpayer files its quarterly income tax returns with the Bureau of Internal Revenue. On the other hand, a taxpayer may also receive or gain other income not directly connected or related to its business activity. As such, the same are subject to the final tax as passive income of the taxpayer.

In this instant case, petitioner is engaged in the business of manufacturing, processing, importing, exporting, buying and selling of electronic equipment, power goods and their accessories. It derives income from its business of buying and selling of these products which it likewise manufactures. In this regard, any income it receives or gains out of these businesses are exempt from the payment of taxes pursuant to its grant of an ITH from the provisions of the PEZA Law.

On the other hand, petitioner's local and foreign currency bank deposits and yields have been earning interests from various banks which cannot be considered as directly connected or related to petitioner's business operations, therefore, must be subject to the final taxes of 20% and 7½%. Section 5, Rule XIII, Part VII[13] of the Implementing Rules and Regulations of Republic Act No. 7916 specifically provides that "incentives granted by the PEZA shall apply only to **registered operations** of the ECOZONE enterprise and only during the period of its registration with PEZA." It is thus erroneous on the part of the petitioner to claim that its interest income, not being entirely and effectively connected with

[13]Incentives to ECOZONE Enterprises, Application and Entitlement.

the conduct of its business, is included under the ITH incentive.

Moreover, this limitation of entitlement to incentives has already been made clear and clarified by Revenue Regulations No. 20-02 dated October 14, 2002, to wit:

REVENUE REGULATIONS NO. 20-02

SUBJECT	:	Clarifying the Tax Treatment of Income Earned from Unregistered Activities by Enterprises Registered under the Bases Conversion and Development Act of 1992 and the Philippine Economic Zone Act of 1995
TO	:	All Internal Revenue Officers and Others Concerned

These Regulations are issued to **clarify** the internal revenue tax treatment of income earned from unregistered activities by enterprises that are registered with the Subic Bay Metropolitan Authority, the Clark Development Authority, or the **Philippine Economic Zone Authority**, as the case may be.

SECTION 1. TAX TREATMENT — Income derived by an enterprise registered with the Subic Bay Metropolitan Authority (SBMA), the Clark Development Authority (CDA), or the Philippine Economic Zone Authority (PEZA) from its registered activity/ies shall be subject to such tax treatment as may be specified in its terms of registration (i.e., the 5% preferential tax rate, the income tax holiday, or the regular income tax rate, as the case may be). Nonetheless, **whatever the tax treatment of said enterprise with respect to its registered activity/ies, income realized by such registered enterprise that is not related to its registered activity/ies shall be subject to the regular internal revenue taxes, such as the 20% final income tax on interest from Philippine Currency bank deposits and yield or any other monetary benefit from deposit substitutes, and from trust funds and similar arrangements, the 7.5% tax on foreign currency deposits and the 5%/10% capital gains tax or ½% stock transaction tax, as the case may be, on the sale of shares of stock.**

Income payments made by a registered enterprise to an entity in the Customs Territory shall not be subject to the preferential tax rates or tax exemption enjoyed by the registered enterprise. Thus, dividends paid to the shareholders of a registered enterprise, interest payments to creditors of such registered enterprise (regardless of any tax provision for grossing up of taxes), and other such payments shall be subject to the appropriate rate of tax imposable on the recipient of such income.

SEC. 2. REPEALING CLAUSE — Section 6 (f) of Revenue Regulations No. 1-95 and the provisions of all other internal revenue issuances inconsistent herewith are hereby repealed, modified or amended accordingly.

> **SEC. 3. EFFECTIVITY** — Except for the second paragraph of Section 1 which is a mere reiteration of the law already enforced, these regulations shall take effect after fifteen (15) days following publication in the Official Gazette or any newspaper of general circulation in the Philippines.
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> (SGD.) **JOSE ISIDRO N. CAMACHO**
> Secretary of Finance
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> Recommending Approval:
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> **(SGD.) GUILLERMO L. PARAYNO, JR.**
> Commissioner of Internal Revenue[14]

In fine, granting that petitioner, through its depository banks, Citibank, BPI and RCBC, may have paid and remitted the amounts of P111,792.07 and US$39,903.57 representing final withholding taxes on interests earned from local currency bank deposits and yield and deposits under the expanded foreign currency deposit system, respectively, for the period covering the first quarter of 2001 to July 2003, the same payment and remittance are not erroneous. Hence, petitioner is not entitled to the refund thereof.

IN VIEW OF THE FOREGOING, this instant Petition for Review is hereby **DENIED** for lack of merit.

SO ORDERED.

CAESAR A. CASANOVA
Associate Justice

WE CONCUR:

ERNESTO D. ACOSTA
Presiding Justice

LOVELL R. BAUTISTA
Associate Justice

[14] Emphasis and underscoring supplied.

CERTIFICATION

Pursuant to Article VIII, Section 13 of the Constitution, 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.

ERNESTO D. ACOSTA
Presiding Justice
Chairman, First Division