REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

FIRST NATIONWIDE ASSURANCE CORPORATION,
Petitioner,

- versus -

C.T.A. CASE NO. 6473

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:
DEC 2 2 2003

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D E C I S I O N

This case involves a claim for refund or issuance of tax credit certificate in the amount of P874,300.00 allegedly representing erroneously withheld 20% final tax on interest income derived by petitioner from its investments in fixed rate treasury notes with maturity of more than five (5) years for the period April 30, 2000 to November 29, 2001.

Petitioner is a corporation duly organized and existing under and by virtue of the laws of the Republic of the Philippines, with principal offices at Yuchengco Tower, 500 Q. Paredes St., Binondo, Manila. (*par. 1, Admitted Facts, page 51, CTA records*).

In 1996, 1998 and 1999, petitioner purchased from Citibank, N.A, and China Banking Corporation (CBC), treasury notes issued by the Bureau of Treasury with the following details:

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Value Date	Selling Bank	Exhibit	Type/ Series No.	ISIN No.	Issue Date	Maturity Date	Par/ Face Amount
07-25-96	Citibank	E-1,F-1	FXTN 7-5	PIBD0703G051	07-25-96	07-25-03	P 4,000,000.00
09-26-96	CBC	E-2,F-2	FXTN #10-1	PIBD1006I010	09-26-96	09-26-06	5,000,000.00
02-17-99	Citibank	E-3,F-4	FXTN 10-4	PIBD1007K042	11-27-97	11-27-07	3,000,000.00
07-17-98	Citibank	E-4,F-5	FXTN 7-9	PIBD0704J092	10-30-97	10-30-04	2,800,000.00

On October 25, 1999, the BIR issued BIR Ruling No. 166-99, providing that the interest income, yield or gain from the sale of bonds, debentures or certificates of indebtedness as deposit substitutes, which are ordinarily subject to 20% final tax under Section 27(D)(1) of the NIRC, should be excluded from the gross income if the bonds, debentures or the certificates of indebtedness have maturities of more than five (5) years.

On January 7, 2000, BIR Ruling No. 016-00 was issued, with the BIR reiterating its stand that "if the maturity period of the bonds issued through the Bureau of Treasury will be more than five (5) years, the gains that may be derived therefrom by the bondholders shall accordingly be exempt from the 20% final withholding tax." The BIR stated further that: "Since the law speaks of the exclusion from gross income of all gains derived from long-term investments, it follows that embraced thereunder are income, yield or interest, which are all synonymous with gains, whether discounted or at a premium. Thus, the exemption applies to interest/coupon or profit from the principal of such long-term regular or SDT bonds complying with the statutory maturity period."

For the period April 30, 2000 to November 29, 2001, petitioner earned interest income from the treasury notes it purchased in the gross amount of P4,371,500.00, which was subjected to 20% final withholding tax by the Bureau of Treasury in the total amount of P874,300.00, broken down as follows:

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Treasury Note ISIN	Interest Payment Date	Total Interest Payable	20% Withholding Tax	Net Amount Paid
PIBD0703G051	26-Jul-00	P 315,000.00	P 63,000.00	P 252,000.00
PIBD0703G051	26-Jul-01	P 315,000.00	P 63,000.00	P 252,000.00
PIBD1006I010	27-Sep-00	P 400,000.00	P 80,000.00	P 320,000.00
PIBD1006I010	26-Mar-01	P 400,000.00	P 80,000.00	P 320,000.00
PIBD1006I010	27-Sep-01	P 400,000.00	P 80,000.00	P 320,000.00
PIBD0704J092	30-Apr-00	P 292,250.00	P 58,450.00	P 233,800.00
PIBD0704J092	03-Nov-00	P 292,250.00	P 58,450.00	P 233,800.00
PIBD0704J092	30-Apr-01	P 292,250.00	P 58,450.00	P 233,800.00
PIBD0704J092	03-Nov-01	P 292,250.00	P 58,450.00	P 233,800.00
PIBD1007K042	27-May-00	P 343,125.00	P 68,625.00	P 274,500.00
PIBD1007K042	29-Nov-00	P 343,125.00	P 68,625.00	P 274,500.00
PIBD1007K042	27-May-01	P 343,125.00	P 68,625.00	P 274,500.00
PIBD1007K042	29-Nov-01	P 343,125.00	P 68,625.00	P 274,500.00
TOTAL		P 4,371,500.00	**P 874,300.00**	P 3,497,200.00

Claiming that the Bureau of Treasury erred in applying the 20% withholding tax on the interest income realized from such treasury notes considering that the said treasury notes have a maturity of more than five years, petitioner, on April 18, 2002, filed with the Large Taxpayers Assessment Division of the Bureau of Internal Revenue, an administrative claim for refund in the amount of P874,300.00.00 (*par. 4, Admitted Facts, page 52, CTA Records*). Petitioner posits that the interest income on its long-term investments constitutes *gain* from the sale of bonds, debentures and certificates of indebtedness with maturities of more than five (5) years as provided under paragraph 7(g) of Section 32(B) of the Tax Code. Accordingly, the said interest income is exempt from the 20% withholding tax on deposits and deposit substitutes.

On April 29, 2002, without waiting for an answer from the respondent, petitioner filed the instant petition for review in order to toll the running of the two-year prescriptive period under the law.

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On the basis of the issues jointly stipulated by the parties, the court is now tasked to resolve the following controversies:

1. Whether or not interest income derived from treasury notes which have a maturity in excess of five (5) years is exempt from the 20% withholding tax;

2. Whether or not the Treasury Notes purchased by petitioner from the Bureau of Treasury from Government Securities Eligible Dealers (GSEDs) can be considered as bonds, debentures or certificates under the Tax Code;

3. Whether or not the Bureau of Treasury paid interest on the Treasury Notes and withheld tax at the rate of 20% of the interest payment in the amount of P874,300.00;

4. Whether or not petitioner is entitled to a refund/tax credit on the amount withheld on such interest payment amounting to P874,300.00; and

5. Whether or not petitioner complied with Section 204 in relation to Section 229 of the National Internal Revenue Code.

The pivotal issue in the case at bar is the proper interpretation of the term *"gains"* as used in Section 32(B)(7)(g) of the Tax Reform Act of 1997. Under the said section, gains realized from the sale or exchange or retirement of bonds, debentures or other certificates of indebtedness with a maturity of more than five (5) years shall not be included in gross income and shall be exempt from taxation. Petitioner interpreted the word "gains" in Section 32(B)(7)(g) as broad enough to include interest income from treasury notes.

To support its view that interest from treasury notes is exempt from 20% final tax, petitioner cited respondent's own rulings, namely, BIR Ruling No. 166-99 dated October

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25, 1999, BIR Ruling No. 016-2000 dated January 7, 2000, and BIR Ruling No. DA-022-01-11-00.

In BIR Ruling No. 166-99, issued on October 25, 1999 and addressed to Aegon Life Insurance (Philippines), Inc., respondent ruled that interest income or yields or gain from the sale of bonds, debentures and certificates of indebtedness with maturities of more than five (5) years are excluded from gross income in accordance with Section 32(B)(7)(g) of the 1997 Tax Code and therefore exempt from the 20% final withholding tax on deposit substitutes. BIR Ruling No. 166-99 states in pertinent part:

> "B. As a general rule, the interest income on currency bank deposit and yield or other monetary benefit from these "deposit substitutes" and similar arrangement derived by banks and non-bank financial intermediaries are being taxed at the final rate of 20% under Section 27(D)(1) of the 1997 Tax Code.
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> However, Section 32(B)(7)(g) of the 1997 Tax Code, provides an exception, thus:
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> "Section 32. Gross Income. —
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> 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:
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> xxx xxx xxx
>
> "(7) Miscellaneous Items. —
>
> xxx xxx xxx
>
> "(g) Gains from the Sale of Bonds, Debentures or other Certificate of Indebtedness. Gains realized from the sale or exchange or retirement of bonds, debentures or other certificate of indebtedness with a maturity of more than five (5) years."

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> The idea therefore, is to still treat bonds, debentures or other certificates of indebtedness as "deposit substitutes" the interest income, yield or gain derived therefrom subject to the 20% final tax under Section 27(D)(1) of the 1997 Tax Code, but exclude said interest income, yield or gain from the gross income if the bonds, debentures or the certificate of indebtedness have maturities of more than five (5) years. Conversely, only the income derived on these debt instruments with maturity of more than five (5) years shall be excluded from the gross income.
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> Furthermore, the term sale is not limited to the subsequent transfer of the instrument but to its origination and issuance, as well. Thus, from the time of its issuance, we should consider the "income" which is actually the amount coming to a person within a specified time, whether as payment for the services, interest, or profit from investment. Its usual synonyms being "gain", "profit", "revenue". (Trefry v. Putnam, 116 N.E. 904, 907 227 Mass. 522, L.R.A. 1917F, 806." (Words & Phrases, Gain, page 11, Permanent Edition 18) (BIR Ruling No. 166-99)

Notwithstanding the abovementioned rulings, we cannot agree with petitioner's contention that interest income on its long term investments in treasury notes should be considered as 'gains' exempt from income tax pursuant to Section 32(B)(7)(g) of the 1997 Tax Code. In a number of cases involving a similar issue ***(Nippon Life Insurance Company of the Philippines, Inc. vs. Commissioner of Internal Revenue, CTA Case No. 6142, February 4, 2002; Malayan Reinsurance Corporation (formerly Eastern General Reinsurance Corporation) vs. Commissioner of Internal Revenue, CTA Case No. 6252, July 24, 2002; Malayan Zurich Insurance Company, Inc. vs. Commissioner of Internal Revenue, CTA Case No. 6251, September 30, 2002; First Nationwide Assurance Corporation vs. Commissioner of Internal Revenue, CTA Case No. 6253, October 3, 2002; Rizal Commercial Banking Corporation vs. Commissioner of Internal Revenue, CTA Case No. 6228, December 4, 2002*** *(with CTA Entry of Judgment dated July 1, 2003)*; ***Malayan Insurance Company, Inc. vs. Commissioner of Internal***

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Revenue, CTA Case No. 6243, December 16, 2002; Tokio Marine Malayan Insurance Company, Inc. [formerly Pan Malayan Insurance Corporation] vs. Commissioner of Internal Revenue, CTA Case No. 6254, January 13, 2003; RCBC Savings Bank, Inc. vs. Commissioner of Internal Revenue, CTA Case No. 6341, May 5, 2003 *(with CTA Entry of Judgment dated July 2, 2003)****; Nippon Life Insurance Company of the Philippines, Inc. vs. Commissioner of Internal Revenue, CTA Case No. 6323, July 24, 2003*** *(with CTA Entry of Judgment October 10, 2003)****; Nippon Life Insurance Company of the Philippines, Inc. vs. Commissioner of Internal Revenue, CTA Case No. 6348, September 12, 2003; Nippon Life Insurance Company of the Philippines, Inc. vs. Commissioner of Internal Revenue, CTA Case No. 6289, September 22, 2003 and Tokio Marine Malayan Insurance Company, Inc. (formerly Pan Malayan Insurance Corporation) vs. Commissioner of Internal Revenue, CTA Case No. 6472, December 1, 2003)***, this court interpreted the word "gains" under Section 32(B)(7)(g) of the 1997 Tax Code in this wise:

> "We take the view that 'gains' as the term is used therein in Section 32(B)(7)(g) of the 1997 Tax Code cannot include interest since it clearly refers to gains from the sale of bonds, debentures and other certificates of indebtedness.
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> "Initially, it must be pointed out that whereas the term 'gains' includes 'interest' as a general rule, this rule cannot be applied to Section 32(B)(7)(g) of the 1997 Tax Code which particularly refers to 'Gains from the Sale of Bonds, Debentures or other Certificate of Indebtedness' in its title and 'Gains realized from the sale or exchange or retirement of bonds, debentures and other certificate of indebtedness with a maturity of more than five (5) years' in its body. Stated otherwise, Section 32(B)(7)(g) of the 1997 Tax Code specifically refers to gains from the sale of bonds, debentures and other certificates of indebtedness as contradistinguished from the term 'gains' in its general sense, which is synonymous to income.

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"From the aforequoted Section 32(A) of the 1997 Tax Code, it is clear that there is a distinction between 'gains derived from dealings in property' and 'interests', which are separately classified as items of gross income. 'Gains realized from the sale or exchange or retirement of bonds, debentures and other certificate of indebtedness' would fall under the category of 'gains derived from dealings in property'. On the other hand, 'interests' would include interest from bonds, debentures and other certificate of indebtedness. Gain realized from the sale or exchange or retirement of bonds, debentures and other certificate of indebtedness and interest from bonds, debentures and other certificate of indebtedness fall under separate and distinct income categories.

"It should be noted that both Sections (24)(B)(1) and 25(A)(2) of the 1997 Tax Code expressly exempt interest derived from certain long-term deposit or investment (covered by Bangko Sentral ng Pilipinas [BSP] certificates and with maturity of five years or more) by citizens, resident aliens and non-resident aliens engaged in trade or business within the Philippines from income tax. However, there is no such exemption from income tax on such interest for corporation, domestic or foreign, under Sections 27 and 28 of the 1997 Tax Code.

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There is a clear distinction between interest from bonds and gain from the sale of bonds. It is only the 'Gains realized from the sale or exchange or retirement of bonds, debentures or other certificate of indebtedness with a maturity of more than five (5) years' that is excluded from gross income and thus exempt from income tax under Section 32(B)(7)(g) of the 1997 Tax Code. Such gains from sale or exchange or retirement of bonds, debentures or other certificate of indebtedness fall within the general category of 'Gains derived from dealings in property' as distinguished from interest from bonds, debentures or other certificate of indebtedness, which fall within the general category of 'Interests' under Section 32(A) of the 1997 Tax Code.

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We believe that if Congress intended to exempt interest from bonds, debentures and other certificates of indebtedness under Section 32(B)(7)(g) of the 1997 Tax Code, it would have done so in clear and specific terms. The fact that it used the term 'Gains from sale' in the aforementioned section, knowing fully well of the reference to interest under Sections 24, 25, 27 and 28 of the 1997 Tax Code shows that it did

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not intend to exempt such interest under the aforementioned Section 32(B)(7)(g).

In the case of ***Nippon Life Insurance Company of the Philippines, Inc., vs. Commissioner of Internal Revenue, CA-G.R. SP No. 69224, November 15, 2002***, the Court of Appeals, in affirming our pronouncement in the appealed case, elucidated, thus:

> "The CTA is absolutely correct. Income is the flow of money to an individual or corporation within a specified time, as payment for services, interests, or profits from investments. Income is the return in money from one's business, labor or capital invested. The famous analogy used by the Supreme Court described property, labor and capital as trees and income as their fruits. Thus, income is synonymous with profit or gain. Nippon used this general concept of income or gain to include interest within the meaning of Section 32(B)(7)(g). This strained interpretation suffers from serious flaws.
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> First, while the Tax Reform Act adhered to the above definition of income, it also classified income into the following categories: compensation for services, income derived from the conduct of business or exercise of profession, gains derived from dealings in property, interest, rents, royalties, dividends, annuities, prizes and winnings, pensions, and a partner's distributive share from net income of a general professional partnership. Section 32(B)(7)(g) clearly refers to gains realized from the sale, exchange or retirement of bonds, among others, with a maturity date of more than five (5) years. There is no reason to confuse gains from sale of bonds with gains in the general sense of income. Nippon argued that the law did not qualify the term "gains" but it is impossible not to see that the law did qualify such term and restricted it to gains from sale of bonds.
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> Section 32(B) enumerates the exclusions from gross income. Exclusions, like tax exemptions, are highly disfavored in law. A person claiming a tax exemption must justify his claim by the clearest terms possible because an exemption from the common burden of taxation is not allowed upon vague implications but on language too plain to be mistaken. In the instant case, Nippon's claimed exclusion runs counter to the plain, unequivocal language of the law. It resorted to the legislative intent behind the provision to justify departure from the literal meaning but we all know this is prohibited. The only intent that must be given effect is the one expressed in the language of the statute. If a statute is clear, plain and free from ambiguity, it must be given its literal meaning and applied without attempted interpretation. To depart from the meaning expressed by the

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> words of the statute is to alter the statute and legislate, not to interpret. A statute which is plain, clear and free from doubt is not subject to construction; there is no need for interpretation, only application.
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> In enacting the Tax Reform Act, the legislature may have intended to develop the capital market and encourage savings in long-term investments but even under the restrictive interpretation that gains under the subject provision means gains from sale of bonds, debentures and other certificates of indebtedness, such legislative intent still finds full expression. Section 32(B)(7)(g) as written and as interpreted by the CTA is still an incentive to the development of the bond market because it excludes gains from sales from the computation of the gross income. This may not be as sweeping as Nippon would have wanted to but it is an incentive nonetheless, which is faithful to the legislative intent. Nippon's all or nothing stance on the exclusion of gains from bonds finds no support in either the language or intent of the law.
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> Nippon's position must have drawn inspiration from the tax exemption of long-term deposits under Section 24(B)(1) and 25(A)(2) of the Tax Reform Act. However, these provisions fall under Chapter III, entitled Tax on Individuals and cover specifically citizens/resident aliens and non-resident aliens, respectively. On the other hand, Chapter IV, the Tax on Corporations does not contain a similar exemption on long-term deposits held by corporations, such as Nippon. Thus, the CTA correctly concluded that interests income on bonds held by corporations are not tax exempt, unlike those held by individuals. This is the law but Nippon could not abide by this and so it attempted to make up for this deficiency in Chapter IV by enlarging the scope of Section 32(B)(7)(g). For these unassailable reasons, the petition must fail."

Rulings issued by the Commissioner of Internal Revenue command respect and weight. However, such rulings are not conclusive upon the courts and will be ignored if found to be erroneous ***(Philippine Bank of Communications vs. Commissioner of Internal Revenue, G. R. No. 112024, January 28, 1999)***.

We conclude in the present case that the aforementioned BIR rulings are erroneous. Such rulings were based on the mistaken belief that the term "gains" as used in Section 32(B)(7)(g) of the 1997 Tax Code include interest ***(Nippon Life Insurance***

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Company of the Philippines, Inc. vs. Commissioner of Internal Revenue, CTA Case No. 6142, February 4, 2002).

It is a well-settled rule of statutory construction that tax exemptions are strictly construed against the taxpayer. Consequently, where Section 32(B)(7)(g) of the Tax Code, which grants tax exemption, is susceptible of a restrictive interpretation, such interpretation must be adopted.

From the above discussions, it is clear that the tax exemption from final withholding tax granted under Section 32(B)(7)(g) of the Tax Code is limited only to the gain from sale of long-term investments. Since the present case involves a claim for refund or issuance of a tax credit certificate of the 20% final tax on interest income earned from investments in long-term treasury notes, the same has no basis in law.

Tax refunds are in the nature of tax exemptions, and as such they are regarded as in derogation of sovereign authority and to be construed *strictissimi juris* against the person or entity claiming the exemption **(*Commissioner of Internal Revenue vs. S.C. Johnson and Son, Inc., 309 SCRA 87; and Commissioner of Customs vs. Court of Tax Appeals, 328 SCRA 822*)**. The power of taxation is a high prerogative of sovereignty, its relinquishment is never presumed and any reduction or diminution thereof with respect to its mode or its rate, must be strictly construed, and the same must be coached in clear and unmistakable terms in order that it may be applied ***(84 C.J.S., pages 659 to 800; cited in Philippine Telegraph and Telephone Corporation vs. Commission on Audit, et al., G.R. No. L-55236, December 12, 1986)***.

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WHEREFORE, in the light of the foregoing, the instant petition for review is hereby **DENIED** for lack of merit.

SO ORDERED.

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

WE CONCUR:

ERNESTO D. ACOSTA
Presiding Judge

LOVELL R. BAUTISTA
Associate Judge

CERTIFICATION

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

ERNESTO D. ACOSTA
Presiding Judge

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