REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

FIRST DIVISION

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THE MANILA BANKING CORPORATION,
Petitioner,

- versus -

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

C.T.A. CASE NO. 7645

Members:

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

Promulgated:

JUN 24 2009; 1:20pm

x - x

DECISION

CASANOVA, *J.*:

THE CASE

This is a Petition for Review filed on June 28, 2007 seeking the cancellation of Assessment Nos. LTDO-122-PTT-2002-00003 for deficiency gross receipts tax and LTDO-122-DS-2002-00005 for deficiency documentary stamp tax in the amounts of P953,418.36 and P525,110.83, respectively, on the ground that the said assessments are not based on law or have prescribed, with an alternative prayer for the cancellation of the surcharges under the assessments, in view of the intricacies and novelty of the issues attending the case.

THE FACTS

Petitioner is a banking corporation, duly organized and existing under Philippine laws, with principal office located at TMBC Building, 6772 Ayala Avenue, Makati City.

Respondent, on the other hand, is the duly appointed Commissioner of Internal Revenue, vested by law with the power to decide disputed assessments, enforce the provisions of the National Internal Revenue Code and other tax laws. He may be served with summons and other court processes at the BIR National Office Building, Diliman, Quezon City.

On May 3, 2007, petitioner received a Formal Letter of Demand and Assessment Notice[1] from the Large Taxpayers District Office-Makati under Assessment Notices No. LTDO-122-PT-2002-00003 for the payment of Gross Receipts Tax (GRT) on petitioner's interest income from its foreign currency deposits with various commercial banks in 2002:

On Shore Income		P8,884,482.99
Gross Receipts Tax		444,274.10
Add:	Surcharge	111,068.53
	Interest	382,075.73
	Compromise Penalty	16,000.00
Deficiency Gross Receipts Tax		**P 953,418.36**

And Assessment No. LTDO-122-DS-2002-00005 for deficiency Documentary Stamp Tax (DST) on client's foreign currency deposits with petitioner in 2002:

[1] Exhibit "A"

Loans	
Time Deposits	P160,226,227.00
Total	P160,226,227.00
Documentary Stamp Tax Due	240,339.34
Add: Surcharge	60,000.84
Interest	208,686.65
Compromise Penalty	16,000.00
Deficiency Documentary Stamp Tax	**P 525,110.83**

Petitioner protested these assessments on May 18, 2007[2] but the protest was denied by respondent in a letter dated May 22, 2007, which was received by petitioner on May 30, 2007.[3] Thus, this Petition for Review was filed on June 28, 2007.

On September 3, 2007, respondent filed his Answer raising the following Special and Affirmative Defenses:

> "6. The assessments in question were made and issued in accordance with law, rules and regulations.
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> 7. Verification disclosed that petitioner has a Gross Onshore Income in the amount of P8,885,482.00 which was not subjected to 5% Gross Receipts Tax imposed under Section 121 of the 1997 Tax Code.
>
> 8. It was discovered that petitioner has Loan Agreements and Certificates of Time Deposit in the total amount of P160,226,227.00 which were not subjected to Documentary Stamp Tax imposed under Section 180 of the 1997 Tax Code.
>
> 9. Income derived by a depository bank under the foreign currency deposit system units from foreign currency transactions, with local commercial banks shall be subject to a final tax of 10%. The phrase 'exempt from all taxes' has definitely been deleted by the Legislators. The amendment by deletion of certain words or phrases in a statute indicates that the legislature intended to change the meaning

[2] Exhibit "B"
[3] Exhibits "C" and "D"

of the statute. Thus, by virtue of such deletion, the payment of 10% final tax on FCDU income does not exempt it from gross receipts tax or other taxes for that matter. There being no effective exemption to speak, then all applicable taxes became due (MBTC vs. CIR, CTA Case No. 6504 October 25, 2006).

10. Section 7 (A), R.A. No. 8424 provides as follows:

> '(A) The provision of Section 17 of Republic Act No. 7906, otherwise known as the 'Thrift Banks Act of 1995' shall continue to be in force and effect only until December 31, 1999.
>
> Effective January 1, 2000 all thrift banks, whether in operation as of that date or thereafter, shall no longer enjoy tax exemption provided under Section 17 of RA No. 7906, thereby subjecting all thrift banks to taxes, fees and charges in the same rate as banks and other financial intermediaries.'

11. All presumption are in favor of the correctness of the tax assessment (Interprovincial Autobus vs. Collector of Internal Revenue, 98 Phil. 290)."

After trial, the case was submitted for Decision on November 13, 2008, following the submission of petitioner's Memorandum on October 30, 2008.

Petitioner maintains that despite the doctrine in taxation that "tax burdens are not to be imposed beyond what the statute expressly and clearly imports, tax statutes being construed *strictissimi juris* against the government", petitioner was assessed DST on all Foreign Currency Deposits (FCDUs) made by its clients in 2002 and Gross Receipts Tax (GRT) on the interest earned by petitioner on its own foreign currency deposits in 2002, when no law or regulation imposes these taxes and even though the assessments were already barred by prescription.

Petitioner argues that Republic Act No. 6426, as amended, granted to all foreign currency deposits, including interest thereof, blanket exemption "from any and all taxes whatsoever". According to petitioner, the subsequent passage of Republic Act No. 8424, imposing 7.5% withholding tax on interest from foreign currency deposits and a 10% withholding tax on the interest from foreign currency transactions of FCDUs did not altogether withdraw all the tax exemptions granted to foreign currency depositors under R.A. 6425, as amended. Petitioner also claims that there was also no showing that the P160,226,227.00 equivalent in foreign currency claimed by respondent as foreign currency time deposits of clients are actually time deposits rather than regular savings accounts. Hence, the assessment of DST on foreign currency deposits of petitioner's depositors has no basis in law. Petitioner also maintains that the assessment of GRT on interest from its foreign currency deposits with other FCDUs likewise has no basis in view of the exemption under R.A. 6426.

Petitioner argues that although the phrase "in lieu of all taxes" or "exempt from all taxes" is absent from Section 27 (D)(3) of the National Internal Revenue of 1997, the absence cannot be interpreted to mean that the blanket exemption (other than the tax income) granted to foreign currency depositors including petitioner, have been totally abrogated. Petitioner claims that its contention is supported by the real intent of the lawmakers as manifested in the Joint Explanatory Statement of the Conference Committee of both houses of Congress, and the discussions between lawmakers recorded in the transcripts of the Bicameral Conference Committee Meetings of the members of the Committees on Ways and Means, as well as the Explanatory Note of Cong. Exequiel Javier for House Bill No. 5246 which he introduced in the House of Representatives to correct the mis-impression created by the absence of the phrase "exempt from all taxes, except taxable income" in RA 8424. House Bill 5246, which later became RA 9294, restored the said phrase.

Finally, petitioner avers that the assessment for DST on foreign currency deposits of clients with petitioner in 2002 and for GRT on petitioner's foreign currency deposits with other FCDUs in 2002 have prescribed. The Formal Letter of Demand assessing said taxes for year 2002 was received by petitioner only on May 3, 2007 more than three (3) years after the said taxes became due, assuming they were due at all.

THE COURT'S RULING

The Court is not swayed by petitioner's ratiocinations.

On the issue of the FCDU's taxability, prior to the amendment introduced by the National Internal Revenue Code (NIRC) of 1997, Section 25(a)(6)(B) of the 1977 Tax Code provides that:

> "**(B) Income derived under the Expanded Foreign Currency Deposit System. – Income derived by a depository bank under the expanded foreign currency deposit system** from foreign currency transactions with non-residents, offshore banking units in the Philippines, local commercial banks including branches of foreign banks that may be authorized by the Central Bank of the Philippines to transact business with foreign currency depository system units and other depository banks under the expanded foreign currency deposit system **<u>shall be exempt from all taxes</u>**, except taxable income from such transactions as may be specified by the Secretary of Finance, upon recommendation of the Monetary Board to be subject to the usual income tax payable by banks: Provided, That interest income from foreign currency loans granted by such depository banks under said expanded system to residents (other than offshore banking units in the Philippines or other depository banks under the expanded system) shall be subject to 10% tax.
>
> Any income of non-residents from transaction with depository banks under the expanded system shall be exempt from income tax." (*Underscoring supplied*)

With the amendments introduced in the NIRC of 1997, the phrase "exempt from taxes" has been deleted, as can be seen from Section 27(D)(3),[4] the provision on Expanded Foreign Currency Deposit Units:

> "**(3) Tax on Income Derived under the Expanded Foreign Currency Deposit System. – Income derived by a depository bank under the expanded foreign currency deposit system** from foreign currency transactions with local commercial banks, including branches of foreign banks that may be authorized by the Bangko Sentral ng Pilipinas (BSP) to transact business with foreign currency depository system units and other depository banks under the expanded foreign currency deposit system, including interest income from foreign currency loans granted by such depository banks under said expanded foreign currency deposit system to residents, shall be subject to a final income tax at the rate of ten percent (10%) of such income.
>
> Any income of nonresidents, whether individuals or corporations, from transactions with depository banks under the expanded system shall be exempt from income tax."

By the clear import of the present law, income derived by a depository bank under the foreign currency deposit units from foreign currency transactions with local commercial banks shall be subject to a final tax of 10%. And the phrase **"exempt from all taxes"** has definitely been deleted by the legislators.

The amendment by deletion of certain words or phrases in a statute indicates that the legislature intended to change the meaning of the statute.[5] It is a basic rule in statutory construction that there is no safer nor better canon of interpretation than that when the language of the law is clear and unambiguous, it should be applied as written.[6]

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[4] *And Section 28 (A)(7)(b) of the same Code.*
[5] *Gloria vs. Court of Appeals 306 SCRA 287.*
[6] *Bank of America NT & SA vs. Court of Appeals 234 SCRA 302.*

Petitioner cannot argue that there was no intent on the part of Congress to delete the phrase "exempt from all taxes". In the August 11, 1997 deliberations of the Senate, anent Section 28(A)(7)(b) of the NIRC of 1997, of which Senator Enrile was the author, this intent was clearly present, to quote:[7]

> "Senator Angara: Yes, Mr. President. Let me move to my next point, and that is the lifting of the preferential tax treatment of FCDUs as well as OBUs.
>
> Mr. President, would this not cause some drastic consequences on offshore as well as foreign currency deposits which I understand today are the prime sources of our current account spending? Many of our exporters depend on this FCDUs and OBUs for their foreign exchange needs, and if we remove the preferential tax treatment that we (sic) have been enjoying all these years, are we not going to drive away the foreign currency deposits and OBUs from our shore?
>
> Senator Enrile: Mr President, money goes to a place where it can make money. Whether we have the tax on FCDUs or OBUs, if depositors can make a margin that is favorable to them, they will be here. Business makes profit because it assumes risk.
>
> I do not subscribe to the theory that these people will run away. In fact, they are saving that because of the announcement we made, on this FCDUs, deposits are flying away from the country. But if we look at the figures, Mr. President, out of a total of P17 billion or so, only a little over P200 million left the country. But, I think, this P200 million left the country to pay for obligations in order to stave off a potential increase in the peso equivalent of the foreign currency obligation, and not because of the effort to tax FCDUs. That is one.
>
> Two, we are not discussing here a problem of competition between pesos and dollars or deutschmark or francs. **We are talking here of equity in taxation, Mr. President. These are the more affluent members of the taxable community and yet, they get away with their tax burden. Another thing that I cannot take is, as a member of this Senate and as a member of the community, that we should tax depositors of our own currency in banks and exclude from taxation depositors of foreign currencies. We are insulting our own currency.**

[7] *Transcript of the Senate Session on the Tax Reform Act on August 11, 1997.*

Senator Angara: Mr. President, I can accept all the reasons given by the sponsor. But this repeal of the exemption to me is a very strong signal that we are changing policies in the middle of the stream. We attracted these FCDUs as well as OBUs on the premise that their income will be subject to special tax or in some cases, the offshore income of FCDUs wil be exempt from any taxation. Now we are saying, 'No, we do not need you anymore.'

Unfortunately, Mr. President based on our representation in the past, they come here and they have transacted business, they have helped exporters and other Filipinos needing foreign exchanges, and now we are saying 'No more'.

Is it not a very drastic message we send to the financial market of the world?

Senator Enrile: Mr. President, it is good that this point was raised by the distinguished gentleman from Aurora.

I would like to put into the *Record* that the exemption of FCDUs from paying income tax in the Philippines as well as the secrecy of their bank deposits was introduced in 1977, on November 21, 1977, under Presidential Decree No. 1246 by the then President Ferdinand E. Marcos. I would like to remind the nation and this Chamber that they have been enjoying this tax concession since then.

But what have they done at a time when we were in crisis? In 1983, 1984, 1985, 1986 all the way to 1990, they all flew away. They left the country. So it is not really a question of taxation that is involved here. It is a question of whether the economy is stable enough, strong enough to lessen the risk. They will withdraw from this country even if we give them all these tax concessions and the secrecy for as long as they feel that they are going to risk their capital because of the economic weakness of the country-not because we are taxing them. They will remain here as other foreign businessmen and the Filipino businessmen will remain in business even if we tax them if they can make money."

Further, the fact remains that Congress passed a new law incorporating the amendment introduced by Senator Enrile. This removed the tax exemption of OBUs and FCDUs on their foreign currency transactions. The intent of Congress to subject

OBUs and FCDUs to tax is thus clear. There being no effective exemption to speak of in this case, all applicable taxes became due.

The enactment of a subsequent law, R.A. 9294, restoring the tax exemption is of no moment. It does not necessarily follow that the true intent of Congress was to keep the tax exemption even during the time when the amendment deleting the phrase "exempt from all taxes" was made. Nor does it follow that the restoration of such exemption would give rise to the retroactive application of the tax exemption of FCDUs and OBUs.

In other words, prior to the effectivity of the subsequent law restoring the subject tax exemption there was no longer a tax exemption to speak of, in view of the amendment removing such exemption.

To reiterate, under the NIRC of 1997, the phrase "shall be exempt from all taxes" relative to FCDUs can no longer be found. And the petitioner's insistence that it is still covered by the tax-exempt provision of the old law is quite absurd and contrary to sound reasoning.[8] The same is diametrically opposed to the clear provision of the law. No statutory construction or interpretation is needed in this case. Rewriting of the law is a forbidden ground that only Congress may tread upon.[9]

Since taxes are the lifeblood of the nation, this Court has always applied the doctrine of strict interpretation in construing claims for tax exemptions. Furthermore, a claim of statutory exemption from taxation should be manifest and unmistakable from the language of the law on which it is based. He who claims an

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[8] *ING Bank v. Commissioner of Internal Revenue, CTA Case No. 6017, March 11, 2002.*
[9] *Supra.*

exception from his share of the common burden of taxation must justify his claim by showing that the legislature intended to exempt him by words too plain to be mistaken.[10]

Accordingly, Section 27(D)(3) cannot be construed to mean that the income derived by the depository banks from FCDU transactions is exempt from all taxes, including DST and GRT. Petitioner's failure to prove that it is exempt from all taxes (except the 10% final tax) means that respondent was correct in assessing petitioner of the applicable DST pursuant to Section 180, and GRT specifically provided under Section 121 of the NIRC, to wit:

> "**SEC. 180. Stamp Tax on All Bonds, Loan Agreements, Promissory Notes, Bills of Exchange, Drafts, Instruments and Securities Issued by the Government or Any of its Instrumentalities, Deposit Substitute Debt Instruments, Certificates of Deposits Bearing Interest and Others Not Payable on Sight or Demand.** — On all bonds, loan agreements, including those signed abroad, wherein the object of the contract is located or used in the Philippines, bills of exchange (between points within the Philippines), drafts, instruments and securities issued by the Government or any of its instrumentalities, deposit substitute debt instruments, certificates of deposits drawing interest, orders for the payment of any sum of money otherwise than at sight or on demand, on all promissory notes, whether negotiable or non-negotiable, except bank notes issued for circulation, and on each renewal of any such note, there shall be collected a documentary stamp tax of Thirty centavos (P0.30) on each Two hundred pesos (P200), or fractional part thereof, of the face value of any such agreement, bill of exchange, draft, certificate of deposit, or note: Provided, That only one documentary stamp tax shall be imposed on either loan agreement, or promissory notes issued to secure such loan, whichever will yield a higher tax: Provided, however, That loan agreements or promissory notes the aggregate of which does not exceed Two hundred fifty thousand pesos (P250,000) executed by an individual for his purchase on installment for his personal use or that of his family and not for business, resale, barter or hire of a house, lot, motor vehicle, appliance or furniture shall be exempt from the payment of the documentary stamp tax provided under this Section."

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[10] *Commissioner of Internal Revenue vs. Court of Appeals, 298 SCRA 83.*

> **"SEC. 121. Tax on Banks and Non-Bank Financial Intermediaries.** - There shall be a collected tax on gross receipts derived from sources within the Philippines by all banks and non-bank financial intermediaries in accordance with the following schedule:
>
> xxx xxx xxx"

Petitioner also argues that the assessment has prescribed. As provided under Section 203 of the 1997 NIRC, the government must assess not later than three (3) years counted from and after the period fixed by law for the filing of the tax return or the date of actual filing, whichever is the later date, subject to exceptions provided under Section 222 of the same code.

On the issue of prescription, Section 203 of the 1997 NIRC provides:

> **"Section 203. Period of Limitation Upon Assessment and Collection.** – Except as provided in Section 222, **internal revenue taxes shall be assessed within three (3) years after the last day prescribed by law for the filing of the return,** and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period: *Provided,* That in a case where a return is filed beyond the period prescribed by law, the three (3)-year period shall be counted from the day the return was filed. For purposes of this Section, a return filed before the last day prescribed by law for the filing thereof shall be considered as filed on such last day." *(Emphasis Supplied)*

Pursuant to the said provision, the three-year period to assess commences from the date of actual filing of the return or from the last date prescribed by law for the filing of such return, whichever comes later. Relative thereto, under Section 128(A)(1) of the NIRC of 1997, in relation to Section 121 of the same Code, Gross Receipts Tax (GRT) returns are filed on a quarterly basis and the tax due thereon paid within twenty five days after the end of each taxable quarter. On the other hand, under Section 200(B) of the same Code, DST returns are filed within ten days after the close of the month when the taxable document was made, signed, issued, accepted or transferred; and the tax thereon must be paid at the same time the said return is filed.

In this case, it is undisputed that petitioner received the Formal Letter of Demand on May 3, 2007, for its unpaid or deficiency DST and GRT for 2002. The same was clearly issued beyond the three-year period prescribed by law within which the respondent could issue an assessment against petitioner.

However, the Court finds merit in respondent's allegation that the ten-year prescriptive period should apply in this case. Section 222 of the NIRC of 1997 provides for exceptions to the period of limitations on the assessment and collection of taxes and applicable is paragraph (a) thereof, which reads:

> "In the case of a **false or fraudulent return with intent to evade tax or of failure to file a return, the tax may be assessed,** or a proceeding in court for the collection of such tax may be filed without assessment, at any time within **ten (10) years after the discovery of the falsity, fraud or omission**: *Provided*, That in a fraud assessment which has become final and executory, the fact of fraud shall be judicially taken cognizance of in the civil or criminal action for the collection thereof." *(Emphasis Supplied)*

Stated differently, in cases of (1) fraudulent returns; (2) false returns with intent to evade tax; and (3) failure to file a return, the period within which to assess tax is ten years from discovery of the fraud, falsification or omission, as the case may be.

With regard to the false or fraudulent returns, it has been consistently held that in order to render a return made by a taxpayer a "false return" within the meaning of Section 222 of the NIRC of 1997, there must appear, a design to mislead or deceive on the part of the taxpayer, or at least culpable negligence. On the other hand, the burden of proving fraud is with respondent, for one of the disputable presumptions provided the Revised Rules of Court is that the law has been obeyed.

In this case, there is no iota of evidence presented by the respondent as to any fraud or falsity on the return with intent to evade payment of tax. Fraud is a question of fact and the circumstances constituting fraud must be alleged and proved. It is never lightly presumed because it is a serious charge.[11]

However, as can be seen from the records and as duly admitted by petitioner, it failed to file a return for both DST and GRT.[12] Hence, respondent correctly argued that due to such failure, the period within which to assess tax is ten years from the discovery of such omission, as provided in Section 222 (a), as above-quoted.

Finally, as regards the correct amount of tax liability, this Court finds partial merit in petitioner's argument. It is stressed that a compromise penalty presupposes an arrangement or agreement between the parties as to the payment of the amount due. The essence of a compromise penalty is mutuality and its unilateral imposition is without legal basis. It is illegal and unauthorized.[13] As mutuality is not present in this case, no compromise penalty may be imposed. Thus, reduction of the amount of petitioner's tax liability by P32, 000.00, representing compromise penalty,[14] is in order.

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[11] *Commissioner of Internal Revenue vs. Ayala Securities Corporation, 70 SCRA 204.*
[12] *Minutes of September 28, 2007 hearing, Docket, p. 45.*
13 *Commissioner of Internal Revenue vs. Lianga Bay Logging Co., 193 SCRA 86, quoting Collector vs. UST, 100 Phil 1062, Phil. International Fair vs. Collector, G.R. Nos. L-12928 and L-12932, March 1962.*
[14] *P16,000 for Assessment No. LTDO-PT-2002-00003 and P16,000 for Assessment No. LTDO-122-DS-2002-00005.*

With such reduction, petitioner's Deficiency Gross Receipts Tax and deficiency Documentary Stamp Tax are computed as follows:

Deficiency Gross Receipts Tax

On Shore Income	P8,884,482.99
Gross Receipts Tax	444,274.10
Add: Surcharge	111,068.53
Interest	382,075.73
Deficiency Gross Receipts Tax	**P 937,418.36**

Deficiency Documentary Stamp Tax

Loans	
Time Deposits	P160,226,227.00
Total	P160,226,227.00
Documentary Stamp Tax Due	240,339.34
Add: Surcharge	60,000.84
Interest	208,686.65
Deficiency Documentary Stamp Tax	**P 509,110.83**

WHEREFORE, premises considered, the instant Petition for Review is **PARTIALLY GRANTED**. The assessment for compromise penalty in the total amount of P32,000.00 is hereby **CANCELLED** for lack of statutory basis. However, petitioner is **ORDERED to PAY** the amount of P937,418.36 representing deficiency Gross Receipts Tax under Assessment Notice No. LTDO-122-PT-2002-00003 and the amount of P509,110.83 representing deficiency Documentary Stamp Tax under Assessment Notice No. LTDO-122-DS-2002-00005, plus twenty (20%) percent delinquency interest per annum, from May 20, 2007, as demanded by respondent in the Formal Letter of Demand pursuant to Section 249 of the NIRC, as amended, until such amount is fully paid.

SO ORDERED.

CAESAR A. CASANOVA
Associate Justice

WE CONCUR:

ERNESTO D. ACOSTA
Presiding Justice

LOVELL R. BAUTISTA
Associate Justice

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