REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

THIRD DIVISION

EGIS ROAD OPERATION S.A.,
Petitioner,

-versus-

THE SECRETARY OF FINANCE and COMMISSIONER OF INTERNAL REVENUE,
Respondent.

CTA Case No. 8414

Members:
BAUTISTA, Chairperson
FABON-VICTORINO, *and*
RINGPIS-LIBAN, *JJ.*

Promulgated:

DEC 15 2016
4:00 p.m.

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DECISION

RINGPIS-LIBAN, *J.*:

This is a Petition for Review filed by EGIS Road Operation S.A. to seek the reversal of the ruling of the Secretary of Finance dated November 15, 2011 which affirmed BIR Ruling No. ITAD 210-11 dated August 15, 2011. The ruling denied petitioner's Tax Treaty Relief Application and declared that the dividends paid to petitioner by Egis Road Operations Philippines, Inc. on May 6, 2010 and on August 31, 2010 are subject to the regular income tax rate of thirty percent (30%) pursuant to Section 28(B)(1) of the National Internal Revenue Code of 1997, as amended.

THE FACTS

Petitioner EGIS Road Operation S.A. ("ERO S.A." for brevity) is a non-resident foreign corporation organized and existing under the laws of France, with principal address at 11 Avenue du Center, 78 280 Guyancourt, France and with Philippine Tax Identification Number 293-638-147-000.[1] ERO S.A. is not registered as a corporation or partnership licensed to do business in the Philippines and it does not do business in the Philippines.[2]

The Commissioner of Internal Revenue (CIR) has previously issued BIR Ruling No. DA-ITAD 037-09 dated March 18, 2009, confirming the preferential tax rate on the payment of dividends received by petitioner from Tollways Management Corporation pursuant to the Convention between the Government of the Republic of the Philippines and the Government of the French Republic for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income.[3]

On April 20, 2010, the Board of Directors of Egis Road Operations Philippines, Inc. ("ERO Philippines" for brevity) approved the declaration of cash dividend in the amount of ₱60,000,000.00, in favor of its stockholders of record as of December 31, 2009 and payable within the year 2010. The Corporate Secretary of ERO Philippines certified that as of April 20, 2010, ERO S.A. is the stockholder of 79,595 common shares of stock of ERO Philippines, with a par value of ₱100.00 per share, or a total par value of ₱7,959,500.00, which is equivalent to 99% of the total issued and outstanding shares of ERO Philippines.[4] ERO Philippines is a corporation organized and existing under the laws of the Philippines, with office address at Unit 703, Citystate Centre, 709 Shaw Blvd., Pasig City.

On August 25, 2010, the CIR issued Revenue Memorandum Order (RMO) No. 72-2010 entitled, "Guidelines on the Processing of Tax Treaty Relief Applications (TTRA) Pursuant to Existing Philippine Tax Treaties" and addressed to all revenue officials and personnel and others concerned. The RMO took effect on November 4, 2010.[5]

On March 18, 2011, ERO S.A. filed with the International Tax Affairs Division (ITAD) of the Bureau of Internal Revenue (BIR) a Tax Treaty Relief Application (TTRA) dated March 17, 2011 to request confirmation that the dividends paid by ERO Philippines to ERO S.A. on May 6, 2010 and on August 31, 2010 are subject to the preferential tax rate of 10% pursuant to the Convention between the Republic of the Philippines and the Government of French Republic for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income ("RP-France Tax Treaty" for

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[1] Stipulated Facts, Joint Stipulation of Facts and Issue (JSFI), docket, p. 594.
[2] *Ibid.*
[3] *Ibid.*
[4] *Ibid.*
[5] *Ibid.*, pp. 594-595.

brevity), as amended by the Protocol to the Tax Convention between the Government of the Republic of the Philippines and the Government of the French Republic effective January 1, 1998.[6]

The said TTRA included the following attachments, which form part of the BIR Records of the case:

a. Consularized certification issued by the tax authority of France to the effect that ERO S.A. is a resident of such country for purposes of the tax treaty being invoked in the tax year concerned;

b. Consularized certification and certified copy of the Articles of Association of ERO S.A. from the issuing agency, office or authority attesting that the copy of Articles of Association is a certified true copy or faithful reproduction thereof;

c. Consularized certification and certified copy of the Certificate of Incorporation of ERO S.A. from the issuing agency, office or authority attesting that the copy of Certificate of Incorporation is a certified true copy or faithful reproduction thereof;

d. Consularized SPA duly executed by the authorized representative of ERO S.A. authorizing Tam-Yap Caga & Associates to file the TTRA of ERO S.A.;

e. Proof of identification of the authorized signatory of ERO S.A. to its SPA;

f. Certification from the Philippine Securities and Exchange Commission that ERO S.A. is not registered to engage in business in the Philippines;

g. Certificate of No Pending Case; and

h. Duly authorized certificate executed by the Corporate Secretary of ERO Philippines showing the details of the dividend declaration, the number, value and type of shares of ERO S.A. as of the date of record/transaction, and as of the date of payment of the subject dividends, the percentage of ownership of ERO S.A. as of the date of record/transaction, and as of the date of payment of the subject

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[6] *Ibid.*, p. 595.

dividends, the acquisition date of the shares of ERO S.A., and the mode of acquisition of the shares of ERO S.A.[7]

On August 15, 2011, the former BIR Commissioner Kim S. Jacinto-Henares issued BIR Ruling No. ITAD 210-11 denying petitioner's application as follows:

"In reply, please be informed that Section 14 and 13 of Revenue Memorandum Order ('RMO') No. 72-2010 which was published in the Manila Bulletin on October 20, 2010, and effective November 4, 2010, provides that:

'*Section 14. WHEN AND WHERE TO FILE THE TTRA.*

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Filing should always be made BEFORE the transaction. Transaction for purposes of filing the TTRA shall mean before the occurrence of the first taxable event

Failure to properly file the TTRA with ITAD within the period prescribed herein shall have the effect of disqualifying the TTRA under the RMO.

'*Section 13. DEFINITIONS. –*

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4. First taxable event *for purposes of filing the Tax Treaty Relief Application (TTRA), shall mean the first or the only time when the income payor is required to withhold the income tax thereon or should have withheld taxes thereon had the transaction been subjected to tax…*'

Under RMO 72-2010, the filing of TTRAs should be made **before** the occurrence of the **first taxable event**, or the first or the only time when an income payor is required to withhold income tax on payments subject to preferential treatment. The *first and only*

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[7] *Ibid.*, pp. 595-596.

time referred herein corresponds to **the period a withholding agent is required to file the necessary returns on final and creditable income taxes withheld in a particular month,** which is **within ten days after the end of that month,** or, if the withholding was made in **December, on or before January 15 of the following year,** pursuant to Section 2.58(A)(2) of **Revenue Regulations No. 2-98 (Implementing Republic Act No. 8424, 'An Act Amending the National Internal Revenue Code, as amended' Relative to the Withholding on Income Subject to the Expanded Withholding Tax and Final Withholding Tax, Withholding of Income Tax on Compensation, Withholding of Creditable Value-Added Tax and Other Percentage Taxes),** thus:

> '*Section 2.58. RETURNS AND PAYMENT OF TAXES WITHHELD AT SOURCE.*
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> *(A) Monthly return and payment of taxes withheld at source –*
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> *xxx xxx xxx*
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> *(2) WHEN TO FILE. –*
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> *(a) For both large and non-large taxpayers, the withholding tax return, whether creditable or final (including final withholding taxes on interest from any currency back deposit and yield or nay other monetary benefit from deposit substitutes and from trust funds and similar arrangements) shall be filed and payments should be made within ten (10) days after the end of each month, except for taxes withheld for the month of* ***December of each year,*** *which shall be filed on or before* ***January 15 of the following year...***" *(Emphasis added)*

Accordingly, since the TTRA in question was filed on **March 18, 2011**, the first taxable event that corresponds to that date falls on or before **April 10, 2011**, as if **ERO Philippines** made a payment in March 2011 and would then file a monthly income tax return thereon until April 10, 2011. With respect to dividends paid by **ERO Philippines** to **ERO S.A.** on any date in the year 2010, or at the latest, **December 31, 2010**, the filing of the corresponding

TTRA should have been made **before January 15, 2011**, pursuant to RMO 72-2010. However, since the TTRA for such dividends paid by **ERO Philippines** to **ERO S.A.** was **not** filed within the prescribed period of filing, such dividends are therefore **disqualified** from the relief being sought for. This being the case, instead of a reduced rate of 10 percent, the dividends paid to **ERO S.A.** are subject to income tax at the regular rate of 30 percent of the gross amount thereof, under Section 28(B)(1)(a) of the National Internal Revenue Code of 1997, as amended, thus:

'Section 28. Rates of Income Tax on Foreign Corporations. –

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(B) Tax on Nonresident Foreign Corporation. –

(1) ***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 interests, dividends, rents, royalties, 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) and (d) above: Provided, That effective January 1, 2009, the rate of income tax shall be thirty percent (30%)'"*[8]

On September 14, 2011, petitioner ERO S.A. appealed to the Department of Finance (DOF) Secretary for the review and reversal of BIR Ruling No. ITAD 210-11 alleging that the ruling is unlawful in view of its retroactive application of the provisions of RMO No. 72-2010 and that the CIR exceeded the granted authority to implement tax treaties by providing, under the terms of the RMO, additional requirements not otherwise stated in the law/treaty that it seeks to implement.[9]

The appeal filed with the DOF Secretary contained the following attachments:

[8] *Ibid.*, pp. 596-599.
[9] *Ibid.*, pp. 599-600.

a. Copy of BIR Ruling No. ITAD 210-11 dated August 15, 2011;

b. Letter request to the BIR dated September 9, 2011 requesting the authenticated copy of the documents submitted to the BIR ITAD on March 18, 2011;

c. Authenticated copies of the documents submitted to the BIR on March 18, 2011;

d. Copy of Revenue Administrative Order No. 03-01;

e. Copy of the Convention between the Republic of the Philippines and the Government of French Republic for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income;

f. Copy of the Protocol to the Tax Convention between the Government of the Republic of the Philippines and the Government of the French Republic, effective January 1, 1998;

g. Copy of BIR Ruling No. DA-ITAD 037-09 dated March 18, 2009 addressed to ERO S.A. confirming the preferential tax rate on the payment of dividends received from Tollways Management Corporation pursuant to the Convention between the Government of the Republic of the Philippines and the Government of the French Republic for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income;

h. Copy of BIR Ruling No. ITAD 034-10 dated September 14, 2010 addressed to ERO S.A. confirming the application of double tax treaty rates on the dividends declared and paid by ERO Philippines;

i. Copy of ITAD Ruling No. 031-04 addressed to Sumitomo Heavy Industries, Ltd. Designing and Manufacturing, Inc. wherein the BIR favorably ruled on the application for the tax treaty for dividends declared and paid on June 6, 2003 prior to the September 16, 2003 request for confirmation;

j. Copy of ITAD Ruling No. 164-02 dated September 23, 2002 wherein the BIR favorably ruled on the application for the tax treaty for dividends declared and paid on June 7, 2002 prior to the July 22, 2002 request for confirmation;

k. Copy of ITAD BIR Ruling No. 058-10 dated October 26, 2010 addressed to Korea Electric Power Corporation wherein the BIR favorably ruled on the application for the tax treaty for dividends declared on April 3, 2009 and July 24, 2009 and the latter paid on July 29, 2009 prior to the October 27, 2009 request for confirmation; and

l. Copy of DA ITAD BIR Ruling No. 099-06 dated August 25, 2006 addressed to Sumitomo Corporation (Sumitomo) and Mitsui & Co. Ltd. (Mitsui) wherein the BIR favorably ruled on the application for the tax treaty for dividends declared on May 9, 2005 and paid on or before June 8, 2005 prior to the November 18, 2005 request for confirmation.[10]

On November 15, 2011, respondent DOF Secretary affirmed the ruling of respondent CIR.[11]

On January 24, 2012, petitioner filed a Petition for Review[12] before the Court of Tax Appeals (CTA).

Respondent CIR filed his Answer[13] on April 3, 2012, while respondent Secretary of Finance filed his Answer[14] on April 30, 2012, essentially raising the following Special and Affirmative Defenses:

1. The petition is procedurally infirm; the subject matter of the present suit is within the jurisdiction of the Regional Trial Court, not the CTA;

2. Assuming for the sake of argument that the CTA has jurisdiction over the instant petition, the same should still be dismissed for failure of petitioner to comply with the procedural requirements for the availment of the preferential tax rate under the RP-France Tax Treaty;

3. RMO No. 72-2010 has prospective application;

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[10] *Ibid.*, pp. 600-601.
[11] *Ibid.*, p. 601.
[12] Docket, pp. 9-44.
[13] Docket, pp. 144-172.
[14] Docket, pp. 181-205.

4. The dividends paid to petitioner are not entitled to the 10% preferential tax rate; and

5. The rulings of the CIR and the Secretary of Finance have the force and effect of law.

The case was set for pre-trial conference on June 15, 2012.[15] After filing their respective Pre-Trial Briefs on June 8, 2012,[16] the parties entered into a Joint Stipulation of Facts and Issues[17]. Thereafter, the pre-trial was terminated and trial on the merits ensued.[18]

Based on the Pre-Trial Order[19] the parties agreed to submit two issues, to wit:

1. Whether or not the Honorable Court of Tax Appeals has jurisdiction over the subject matter of the instant case; and

2. Whether or not the Dividends paid by ERO Philippines to petitioner are subject to 10% Preferential Rate provided under the RP-France Double Tax Treaty.

During the initial presentation of petitioner's evidence, counsel for respondent Secretary of Finance moved for the early resolution of the issue on jurisdiction.[20]

Subsequently, both respondents Secretary of Finance and CIR filed their Motions to Dismiss[21] assailing the Court's authority to hear and determine the petition. According to respondents, the subject matter of the case falls within the jurisdiction of the Regional Trial Courts and not within the CTA's special jurisdiction. The authority conferred upon the CTA under Section 7 of Republic Act (RA) No. 1125, as amended, does not include jurisdiction over cases where the constitutionality of a law or rule is challenged.

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[15] Notice of Pre-Trial Conference issued on May 18, 2012, docket, p. 208.
[16] Petitioner's Pre-Trial Brief, docket, pp. 209-219; Respondent Secretary of Finance's Pre-Trial Brief, docket, pp. 220-228; and Respondent CIR's Pre-Trial Brief, docket, pp. 231-236.
[17] Docket, pp. 255-266.
[18] Resolution dated August 28, 2012, docket, p. 268.
[19] Docket, pp. 271-280.
[20] Minutes of the Hearing, docket, p. 298.
[21] Respondent Secretary of Finance's Motion to Dismiss was filed on November 27, 2012, docket, pp. 301-314; Respondent CIR's Motion to Dismiss was filed on November 28, 2012, docket, pp. 317-339.

Meanwhile, petitioner opposed the dismissal of the case. In its Comment[22], petitioner claims that the petition seeks a review of the Decision or ruling of the Secretary of Finance dated November 15, 2011 which affirmed BIR Ruling No. ITAD 210-11 dated August 15, 2011 and the constitutionality of the Revenue Memorandum Order is but one of the issues raised in the petition. According to petitioner, the CTA may just ignore the constitutionality issue and resolve the other issues raised in the petition. Further, the CTA has exclusive appellate jurisdiction to review by appeal the decisions of respondent CIR involving matters arising under the NIRC, as stated in Section 7(a)(1) of RA No. 1125, as amended, or a decision or ruling of the Secretary of Finance.

In the Resolution[23] promulgated on March 22, 2013, the CTA First Division ruled that it has jurisdiction over the nature and subject matter of the instant petition. Since this case was instituted for the Court to review the decision or ruling of the Secretary of Finance dated November 15, 2011 that affirmed the ruling of the CIR in BIR Ruling No. ITAD 210-11 dated August 15, 2011, the Court needs only to refrain from ruling over the issues on the validity or constitutionality of the RMO. Hence, respondents' Motions to Dismiss were denied for lack of merit.

Both respondents filed their Motions for Reconsideration[24], but were denied in the Resolution[25] promulgated on July 3, 2013.

Meanwhile, in view of Administrative Circular No. 01-2013 dated March 26, 2013, reorganizing the three Divisions of the CTA, and the Order of the CTA First Division dated April 5, 2013, this case was transferred to the CTA Third Division.[26]

When the case was called for the initial presentation of evidence for petitioner, counsel for respondents moved for the suspension of the proceedings on the ground that respondents filed a Petition for Certiorari with the Supreme Court to annul the Resolution dated March 22, 2013.[27]

Respondents filed a Joint Motion to Suspend[28] the proceedings before the CTA in view of their filing of a Petition for Certiorari (with Urgent Prayer for the Issuance of a Temporary Restraining Order and/or Writ of Preliminary Injunction) with the Supreme Court. For practical and ethical considerations,

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[22] Docket, pp. 368-378.

[23] Docket, pp. 382-391.

[24] Respondent CIR's Motion for Reconsideration was filed on May 2, 2013, docket, pp. 395-409; Respondent Secretary of Finance's Motion for Reconsideration was filed on May 6, 2013, docket, pp. 411-424.

[25] Docket, pp. 450-454.

[26] Resolution dated April 19, 2013, docket, p. 394.

[27] Minutes of the Hearing, docket, p. 467.

[28] Docket, pp. 498-504.

the Court granted the motion and suspended the proceeding in the observance of judicial courtesy.[29]

In the Resolution[30] dated December 10, 2014, the Supreme Court denied respondents' petition and ruled that the CTA has jurisdiction to hear the case citing *City of Manila vs. Judge Grecia-Cuerdo.* The CTA was then ordered to proceed expeditiously with the proceedings.

On March 23, 2015, the Supreme Court's Resolution dated December 10, 2014 became final and executory.[31]

On September 22, 2015, the Court continued the proceedings but the parties manifested that they would no longer present evidence since the only issue in this case is whether the dividends are subject to the 10% preferential rate.[32]

The parties submitted anew their Joint Stipulation of Facts and Issue.[33]

The case was then submitted for decision on January 18, 2016,[34] after respondents' submitted their Memoranda[35] on December 2, 2015 and on January 4, 2016, and after petitioner filed its Memorandum[36] on January 4, 2016.

THE ISSUE[37]

The sole issue for this Court's resolution is whether or not the dividends paid by ERO Philippines to petitioner are subject to the 10% preferential rate provided under the RP-France Tax Treaty.

THE RULING OF THE COURT

The issue regarding the Court's jurisdiction to hear the instant petition was settled in the Resolutions[38] dated March 22, 2013 and July 3, 2013, the pertinent portions of which read as follows:

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[29] Resolution dated November 7, 2013, docket, pp. 565-567.
[30] Docket, pp. 584-585.
[31] Entry of Judgment, docket, p. 575.
[32] Minutes of the Hearing, docket, p. 590.
[33] Docket, pp. 593-605.
[34] Docket, p. 711.
[35] Docket, pp. 609-622 and 684-707.
[36] Docket, pp. 663-682.
[37] JSFI, docket, p. 602.
[38] Docket, pp. 382-391 and 450-454.

> "To repeat, there is no dispute that Section 7 of R.A. No. 1125, as amended, is the pertinent law governing the jurisdiction over the instant case which provides that the Court has jurisdiction over '**Decisions of the Commissioner of Internal Revenue in cases involving** disputed assessments, refunds of internal revenue taxes, fees or other charges, penalties imposed in relation thereto, or **other matters arising under the National Internal Revenue Code or other laws or part of law administered by the Bureau of Internal Revenue.**'
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> Again, the subject of the case is the decision of the respondent CIR holding petitioner liable for tax under the regular rate of 30% on its dividends received from Egis Road Philippines. Under Section 7 or R.A. No. 1125, as amended, such decision of the CIR is appealable to this Court."[39]

The Court's ruling was sustained in the Supreme Court's Resolution[40] dated December 10, 2014, it reads:

> "The CTA has the power to determine 'whether or not there has been grave abuse of discretion amounting to lack or excess of jurisdiction on the part of the RTC in issuing an interlocutory order in cases falling within the exclusive appellate jurisdiction of the tax court.' This involves a petition for certiorari involving the question whether or not the CTA acted arbitrarily in denying the motion to dismiss in an action involving an assessment of income tax. Our recent decision in *City of Manila v. Judge Grecia-Cuerdo* is therefore applicable.
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> **ACCORDINGLY**, the petition is hereby **DENIED**. The Court of Tax Appeals is hereby ordered to proceed expeditiously with the proceedings in CTA Case No. 8414. xxx"

Considering the foregoing, the Court shall now determine the correctness of respondents' ruling that the dividends paid to petitioner by ERO Philippines on May 6, 2010 and on August 31, 2010 are subject to the regular income tax rate of thirty percent (30%) pursuant to Section 28(B)(1) of the National Internal Revenue Code of 1997, as amended, and not to the ten percent (10%) preferential tax rate under the provisions of the RP-France Tax Treaty.

[39] Docket, p. 453.
[40] Docket, pp. 584-585.

In the assailed ruling of the Secretary of Finance dated November 15, 2011 and BIR Ruling No. ITAD 210-11 dated August 15, 2011, petitioner's TTRA was denied and accordingly disqualified the application of the 10% preferential tax rate on dividends received from ERO Philippines for the sole reason that its TTRA was filed beyond the period prescribed under RMO No. 1-2000 and RMO No. 72-2010.

According to respondents, petitioner did not observe the requisite period as it filed its TTRA on March 18, 2011 or **after** the payment of dividends on May 6, 2010 and August 31, 2010. For this reason, petitioner was disqualified from availing of the 10% preferential tax rate.

Under RMO No. 1-2000, any availment of the 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 sought.

Meanwhile, RMO No. 72-2010 requires the taxpayers to file the TTRA before the occurrence of the first taxable event, and failure to properly file the TTRA with ITAD within the prescribed period shall have the effect of disqualifying the TTRA under the RMO. It says:

> "SUBJECT: Guidelines on the Processing of Tax Treaty Relief Applications (TTRA) Pursuant to Existing Philippine Tax Treaties
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> TO: All Revenue Officials and Personnel and Others Concerned
>
> xxx xxx xxx
>
> SECTION 14. *When and Where to File the TTRA.* – All tax treaty relief applications (updated BIR Forms No. 0901-D, 0901-I, 0901-R, 0901-P, 0901-S, 0901-T, 0901-O and 0901-C) relative to the implementation and interpretation of the provisions of Philippine tax treaties shall only be submitted to and received by the International Tax Affairs Division (ITAD). If the forms or any necessary documents are submitted to any other BIR Office, the application shall be considered as improperly filed.

> **Filing should always be made BEFORE the transaction. Transaction for purposes of filing the TTRA shall mean before the occurrence of the first taxable event.**
>
> **Failure to properly file the TTRA with ITAD within the period prescribed herein shall have the effect of disqualifying the TTRA under this RMO.**" *(Emphasis supplied)*

Both RMO No. 1-2000 and RMO No. 72-2010 require a prior TTRA before availment of the tax treaty relief, but only the latter imposes a penalty of disqualification in case of belated filing of TTRA.

If we are to strictly apply the procedure under RMO No. 72-2010, it would result in absurdity because the said rule requires the filing of TTRA **before** the occurrence of the first taxable event. The first taxable events in this case happened on May 6, 2010 and on August 31, 2010. Petitioner could not have known the new rule considering that the declaration of dividends on April 20, 2010 and the payment of dividends on May 6, 2010 and on August 31, 2010 were all prior to the effectivity of RMO No. 72-2010, which took effect only on November 4, 2010. A more important rule of statutory construction dictates that laws should be construed in a manner that avoids absurdity or unreasonableness.[41]

If at all, the applicable administrative policy and procedure on TTRA, given the factual antecedents of this case, is RMO No. 1-2000 which requires the filing of TTRA **at least 15 days before the transaction**. However, it has long been settled that a prior TTRA is not necessary before a taxpayer can avail of the preferential tax treatments under Philippine tax treaties. The Supreme Court in *Deutsche Bank AG Manila Branch vs. Commissioner of Internal Revenue*[42] squarely addressed the issue of "whether the failure to strictly comply with RMO No. 1-2000 will deprive persons or corporations of the benefit of a tax treaty." The High Court recognized the superiority of tax treaty over an administrative issuance:

> "Our Constitution provides for adherence to the general principles of international law as part of the law of the land. The time-honored international principle of *pacta sunt servanda* demands the performance in good faith of treaty obligations on the part of the states that enter into the agreement. Every treaty in force is binding upon the parties, and the obligations under the treaty must

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[41] *Microsoft Corporation vs. Rolando D. Manansala and/or Mel Manansala, doing business as Dataman Trading Company and/or Comic Alley*, G.R. No. 166391, October 21, 2015.

[42] G.R. No. 188550, August 28, 2013.

be performed by them in good faith. More importantly, treaties have the force and effect of law in this jurisdiction.

Tax treaties are entered into 'to reconcile the national fiscal legislations of the contracting parties and, in turn, help the taxpayer avoid simultaneous taxations in two different jurisdictions. *CIR v. S.C. Johnson and Son, Inc.* further clarifies that 'tax conventions are drafted with a view towards the elimination of international juridical double taxation, which is defined as the imposition of comparable taxes in two or more states on the same taxpayer in respect of the same subject matter and for identical periods. The apparent rationale for doing away with double taxation is to encourage the free flow of goods and services and the movement of capital, technology and persons between countries, conditions deemed vital in creating robust and dynamic economies. Foreign investments will only thrive in a fairly predictable and reasonable international investment climate and the protection against double taxation is crucial in creating such climate.' Simply put, tax treaties are entered into to minimize, if not eliminate the harshness of international juridical double taxation, which is why they are also known as double tax treaty or double tax agreements.

'A state that has contracted valid international obligations is bound to make in its legislations those modifications that may be necessary to ensure the fulfillment of the obligations undertaken.' Thus, laws and issuances must ensure that the reliefs granted under tax treaties are accorded to the parties entitled thereto. The BIR must not impose additional requirements that would negate the availment of the reliefs provided for under international agreements. More so, when the RP-Germany Tax Treaty does not provide for any pre-requisite for the availment of the benefits under said agreement.

Likewise, it must be stressed that there is nothing in RMO No. 1-2000 which would indicate a deprivation of entitlement to a tax treaty relief for failure to comply with the 15-day period. We recognize the clear intention of the BIR in implementing RMO No. 1-2000, but the CTA's outright denial of a tax treaty relief for failure to strictly comply with the prescribed period is not in harmony with the objectives of the contracting state to ensure that the benefits granted under tax treaties are enjoyed by duly entitled persons or corporations.

Bearing in mind the rationale of tax treaties, the period of application for the availment of tax treaty relief as required by RMO No. 1-2000 should not operate to divest entitlement to the relief as it would constitute a violation of the duty required by good faith in complying with the tax treaty. The denial of the availment of tax relief for the failure of a taxpayer to apply within the prescribed period under the administrative issuance would impair the value of the tax treaty. At most, the application for a tax treaty relief from the BIR should merely operate to confirm the entitlement of the taxpayer to the relief.

The obligation to comply with a tax treaty must take precedence over the objective of RMO No. 1-2000. Logically, noncompliance with tax treaties has negative implications on international relations, and unduly discourages foreign investors. While the consequences sought to be prevented by RMO No. 1-2000 involve an administrative procedure, these may be remedied through other system management processes, e.g., the imposition of a fine or penalty. But we cannot totally deprive those who are entitled to the benefit of a treaty for failure to strictly comply with an administrative issuance requiring application for tax treaty relief." *(Emphasis supplied)*

In the recent case of *Air Canada vs. Commissioner of Internal Revenue*[43], the Supreme Court recognized the binding effects of a tax treaty and upheld its provisions over that of the NIRC, to wit:

"A tax treaty is an agreement entered into between sovereign states 'for purposes of eliminating double taxation on income and capital, preventing fiscal evasion, promoting mutual trade and investment, and according fair and equitable tax treatment to foreign residents or nationals.' *Commissioner of Internal Revenue v. S.C. Johnson and Son, Inc.* explained the purpose of a tax treaty:

The purpose of these international agreements is to reconcile the national fiscal legislations of the contracting parties in order to help the taxpayer avoid simultaneous taxation in two different jurisdictions. More precisely, the tax conventions are drafted with a view towards the elimination of *international juridical double taxation*, which is defined as the imposition of

[43] G.R. No. 169507, January 11, 2016.

> comparable taxes in two or more states on the same taxpayer in respect of the same subject matter and for identical periods.
>
> The apparent rationale for doing away with double taxation is to encourage the free flow of goods and services and the movement of capital, technology and persons between countries, conditions deemed vital in creating robust and dynamic economies. Foreign investments will only thrive in a fairly predictable and reasonable international investment climate and the protection against double taxation is crucial in creating such a climate. (Emphasis in the original, citations omitted)

Observance of any treaty obligation binding upon the government of the Philippines is anchored on the constitutional provision that the Philippines 'adopts the generally accepted principles of international law as part of the law of the land[.]' *Pacta sunt servanda* is a fundamental international law principle that requires agreeing parties to comply with their treaty obligations in good faith.

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While petitioner is taxable as a resident foreign corporation under Section 28(A)(1) of the 1997 National Internal Revenue Code on its taxable income from sale of airline tickets in the Philippines, *it could only be taxed at a maximum of 1 1/2% of gross revenues,* pursuant to Article VIII of the Republic of the Philippines-Canada Tax Treaty that applies to petitioner as a 'foreign corporation organized and existing under the laws of Canada[.]'

Tax treaties form part of the law of the land, and jurisprudence has applied the statutory construction principle that specific laws prevail over general ones."

Thus, the application of the provisions of the NIRC is subject to the provisions of tax treaties entered into by the Philippines with foreign countries. Since there is a tax treaty being implored in this case, *i.e.*, RP-France Tax Treaty, the same shall be taken into consideration in order to determine the proper tax rate.

Under the RP-France Tax Treaty, the tax rates on dividends are as follows:

"ARTICLE 10
Dividends

1. Dividends paid by a company which is a resident of a Contracting State to a resident of the other Contracting State may be taxed in that other State.

2. However, such dividends may be taxed in the Contracting State of which the company paying the dividends is a resident, and according to the law of that State, but if the recipient is the beneficial owner of the dividends the tax so charged shall not exceed:

   a) 15 per cent of the gross amount of the dividends if the recipient is a company (excluding partnership) which holds directly at least 10 per cent of the voting shares of the company paying the dividends;

   b) in all other cases, 25 per cent of the gross amount of the dividends.

This paragraph shall not affect the taxation of the company in respect of the profits out of which the dividends are paid."

Subsequently, the tax rates were amended through the issuance of the Protocol to the Tax Convention Between The Government of the Republic of the Philippines and The Government of the French Republic signed on January 9, 1976, to wit:

"ARTICLE 5

In Article 10 of the Convention:

— in paragraph 2, the rates of '15 percent' and '25 percent' are replaced respectively by '10 percent' and '15 percent';

— in paragraph 6, the rate of '15 percent' is replaced by '10 percent'.

According to the treaty, dividends may be taxed in the Contracting State of which the company paying the dividends is a resident, and according to the law of that State; but if the recipient is the beneficial owner of the dividends, the tax so charged shall not exceed 10% of the gross amount of the dividends if the recipient is a company (excluding partnership) which holds directly at least 10% of the voting shares of the company paying the dividends.

Based on the stipulated facts, it was established that:

a. petitioner is a non-resident foreign corporation organized and existing under the laws of France;

b. petitioner is not registered as a corporation or partnership licensed to do business in the Philippines and it does not do business in the Philippines; and

c. the Corporate Secretary of ERO Philippines certified that as of April 20, 2010, ERO S.A. is the stockholder of 79,595 common shares of stock of ERO Philippines, with a par value of ₱100.00 per share, or a total par value of ₱7,959,500.00, which is equivalent to 99% of the total issued and outstanding shares of ERO Philippines.

Applying the foregoing, petitioner is qualified to avail of the 10% preferential tax rate on dividends received from ERO Philippines on May 6, 2010 and on August 31, 2010.

WHEREFORE, premises considered, the Petition for Review is **GRANTED**. Accordingly, the ruling of the Secretary of Finance dated November 15, 2011 and BIR Ruling No. ITAD 210-11 dated August 15, 2011 are **REVERSED** and **SET ASIDE**.

SO ORDERED.

Ma. Belen

MA. BELEN M. RINGPIS-LIBAN
Associate Justice

WE CONCUR:

(*On Leave*)
LOVELL R. BAUTISTA
Associate Justice

ESPERANZA R. FABON-VICTORINO
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.

ESPERANZA R. FABON-VICTORINO
Associate Justice
Acting 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