REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

FIRST DIVISION

AMKOR/ANAM PILIPINAS, INC.,
Petitioner,

- versus -

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

C.T.A. CASE NO. 5953

Members:

ACOSTA E. Chairman
BAUTISTA, and
CASANOVA, JJ.

Promulgated:
DEC 2 8 2004

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DECISION

ACOSTA, J.:

This case involves tax deficiency assessments covering taxable year 1994 made by respondent against petitioner in the amount of P258,670,785.57 consisting of withholding tax, value-added tax and documentary stamp tax deficiencies in the amount of P211,816,184.20, P10,952,417.75 and P35,902,183.62, respectively. The petitioner seeks the cancellation of the above disputed tax assessments inclusive of increments.

The facts of the case as culled from the records and evidence are as follows:

Petitioner is a domestic corporation engaged in the business of manufacturing, assembling for a fee, exporting, buying and/or selling semiconductor products and

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components and holds office at the NSC Compound, Km. 22 East Service Road, South Superhighway, Muntinlupa City *(Paragraphs 1 and 2, Petition for Review)*.

On January 6, 1999, petitioner received Demand Letters with accompanying Assessment Notices from respondent, through the Assessment Division of Revenue Region No. 8 (Makati), informing petitioner of its alleged deficiency withholding, documentary stamp and value-added tax liabilities inclusive of increments for the year 1994 in the aggregate amount of P258,670,785.57 *(Paragraph 4, Joint Stipulation of Facts and Issues)*.

On January 25, 1999, the petitioner through its counsel, filed a formal written protest with the respondent assailing the above-mentioned deficiency tax assessments on both factual and legal grounds, together with the documents in support of its arguments and defenses against the validity of the assessment *(Annex "D", Petition for Review)*.

On March 26, 1999, within sixty (60) days after petitioner filed its formal protest, it submitted to the Revenue Region No. 8, Assessment Division additional supporting documents *(Paragraph 6, Joint Stipulation of Facts and Issues)*.

The respondent, however, failed to act upon the said protest within a period of one hundred eighty (180) days from his receipt of petitioner's additional supporting documents. Hence, petitioner was constrained to seek recourse before this Court, by way of this instant Petition for Review.

In his Answer filed on December 9, 1999, respondent asserted the following Special and Affirmative Defenses, to wit:

> "4. Section 110 (b) of the Tax Code provides;
>
> "Sec.110. Value-added tax on sale of goods x x x
>
> (b) Transaction deemed sale

x x x

(4) Retirement from or cessation of business, with respect to inventories of taxable goods existing as of such retirement or cessation."

When petitioner purchased all the interest of Integrated MicroElectronics, Inc. over Automated MicroElectronics, Inc., it is deemed to have purchased also the inventories and real properties considering that there was a change of ownership. Under the above-cited provision of the Tax Code, the said transaction is deemed sale for purposes of VAT.

5. Investigation conducted revealed that petitioner failed to pay the documentary stamp tax on the export sales remittances due under Section 181 of the Tax Code.

Records further show that petitioner willfully connived with its bank and its mother company to evade the payment of documentary stamp tax.

6. Petitioner must show proof that it paid documentary stamp tax due on the increase of its capitalization through the issuance of common and preferred shares of stock.

7. Petitioner must show proof that indeed it paid the documentary stamp tax due under Section 180 of the Tax Code on its USD 5M loan from the Bank of the Philippine Islands.

8. The floating rate notes which petitioner claims to be debt instruments are actually equity investment, in which case, Section 25 (B)(5) of the Tax Code shall not apply.

9. Petitioner failed to show proof that it withheld the expanded withholding tax due on the rental payment it made on the property it rented from Ms. Vilma Santos-Recto for the use of petitioner's expatriates.

10. Petitioner failed to show that it withheld the corresponding taxes due on the income payment granted to expatriates, such as tuition fees for their dependents and housing benefit as mentioned in the preceding paragraph hereof.

11. Petitioner likewise failed to show proof of withholding and remittance of the interest payment it made on its loan from Advance Micro Devices, Inc.

12. There was no proof to show that petitioner withheld and remitted the 1% tax as provided in Revenue Regulations 12-94 on

the payment it made on its canteen concessionaire (Kopper Kettle), bus service contractor and to the entity giving its employees and officers annual medical check-up.

13. Petitioner failed to pay creditable withholding tax and documentary stamp tax on the land transfer from Integrated MicroElectronics, Inc. (IMI) to IRI, Inc. in payment of shares of stock, on the indirect transfer of land from IRI to petitioner, on the indirect transfer of building from IMI to petitioner, and on the indirect transfer of land and building from petitioner to Salcedo Sunvar Realty.

14. Petitioner failed to withhold the tax due on the payment of legal fees to the foreign affiliate of Bito Lozada & Castillo Law Office.

15. Petitioner failed to withhold the tax due on the remuneration, in the form of advances without proof of liquidation, to expatriates whose employment is not properly documented.

16. The assessment was issued in accordance with law and regulations.

17. All presumptions are in favor of the correctness of tax assessments (**CIR vs. Construction Resources of Asia, Inc.,** *145 SCRA 67*), and the burden to prove otherwise is upon petitioner."

During the course of the trial, the parties decided to stipulate on the issues to be resolved by the Court, namely:

1. Whether or not Petitioner's purchase of all the interest of Integrated MicroElectronics, Inc. over Automated MicroElectronics, Inc. is subject to VAT;

2. Whether or not the communication of petitioner to its non-resident customer, T.L.Ltd., for the inward remittance of the latter's assembly fees is an order of payment subject to the DST under Section 181 of the Tax Code.

3. Whether Petitioner withheld the expanded withholding tax due on the rental payment it made on the property it rented from Ms. Vilma Santos-Recto for the use of Petitioner's expatriates;

4. Whether Petitioner withheld the corresponding taxes due on the income benefits granted to expatriates, such as tuition fees for their dependents and housing benefits;

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5. Whether Petitioner withheld and remitted the tax on interest payment it made on its loan from Advance Micro Devices, Inc. and whether the proper tax rate to be used is 15% pursuant to the RP-US Tax Treaty or 20% pursuant to the Tax Code;

6. Whether Petitioner is liable to withhold and remit 1% tax on the payment to its bus service contractor (PJC), as well as payments made to medical doctors who render medical services for the annual medical examination of company employees;

7. Whether or not Petitioner's payment to Copper Kettle canteen operator representing the cash equivalent of the meal tickets presented by the employees, as well as the payment of its gas, water and electricity consumption is subject to 1% expanded withholding tax;

8. Whether the guaranteed floating rate notes (GFRNs) issued by Petitioner are equity investments the interest on which is subject to 35% income tax on non-resident foreign corporations;

9. Whether or not the professional fees of P2,800,000 were in fact paid by petitioner to a non-resident legal retainer, an affiliate of Bito, Lozada and Castillo Law Office;

10. Whether the DST due on the USD5,000,000 loan obtained by Petitioner from the Bank of the Philippine Islands (BPI) is already paid;

11. What is the rate of DST to be imposed on the 3,446,476 preferred shares issued by Petitioner to IMI;

12. Whether the 46,700,000 shares of common stock being assessed for DST was an original issuance by Petitioner or in fact a sale of shares between AMD and T.L. Ltd.;

13. Whether or not there was in fact a payment of P52,762,407.39 made to a non-resident alien, T.L. Ltd., and for which Petitioner is liable to withhold taxes;

14. Whether Integrated MicroElectronics, Inc. (IMI) transferred land to IMI Realty, Inc. (IRI) in exchange for shares of stock; whether there was indirect transfer of land from IRI to Petitioner, indirect transfer of building from IMI to Petitioner, and indirect transfer of land and building from Petitioner to Salcedo Sunbar Realty. If so, whether the corresponding creditable withholding tax and DST were paid on each alleged transaction. (*Joint Stipulation of Facts and Issues, page 102, CTA Records*)

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We now proceed to answer the first issue.

Respondent, through the revenue examiner alleged that the transaction entered into by petitioner and Integrated MicroElectronics, Inc. (IMI) for the purchase of the its entire shareholdings in Automated Micro Electronics, Inc. (AME) resulted in the transfer by AME of all its finished goods, work-in-process, raw materials, and supplies to petitioner. The respondent proceeded to impose thereon 10% value-added tax (VAT) citing as legal basis Section 100 of the Tax Code of 1993, which requires the payment of 10% VAT on sales, barters or exchanges of goods, or transactions that are deemed sale for VAT purposes.

To resolve this issue, it is best to provide its factual backdrop.

On December 2, 1993, the petitioner entered into an Agreement of Purchase and Sale of Stock with IMI for the purchase of the latter's entire shareholdings in AME, consisting of 400,000,000 shares for a total consideration of P130,000,000 payable partly in cash and partly through the issuance of petitioner's preferred shares to IMI. The transaction resulted in AME becoming petitioner's wholly owned subsidiary.

Clearly, from the foregoing, the transaction between petitioner and IMI did not involve a direct sale or transfer of goods, much less a sale of inventories as alleged by the respondent. The transaction resulted merely in petitioner gaining ownership of the equity of AME, while IMI, its former owner, acquired equity in petitioner in the form of preferred stock.

Further, Section 100(b) cannot be invoked because the transaction between petitioner and IMI does not fall under any of the situations contemplated therein. Perhaps the only item in Section 100(b) that might hint to cover a deemed sale transaction with respect to inventories of taxable goods is Paragraph 4, when the "deemed" seller retires from business or otherwise ceases operations. In the instant case, neither petitioner nor AME ceased to do business despite petitioner's acquisition of 100% equity of AME *(AME's Financial Statements and Income Tax Returns for the taxable years 1993 to 1998, Exhibits "GGG" to "RRR", TSN of Ms. Gemma Merin, April 21, 2003, pp. 15-19).*

In addition, the Tax Code and all relevant revenue issuances are clear that the 10% VAT is imposed upon, and is a direct liability of, the seller of goods. This is unequivocally provided in Section 100(a) of the Tax Code of 1993 when it states that such tax shall "be paid by the seller or transferor". Inasmuch as the petitioner in this transaction was the buyer and not the seller, it could not be held liable for the VAT if any is so due.

Even the contractual arrangements between petitioner and IMI recognize the above provision of Section 100(a) as shown in Section 8.4 of the Purchase and Sale of Stock Agreement *(Exhibit "A")* between the parties which states, among others, that:

> **"SELLER [IMI] shall bear all sales, transfer, documentary stamp duty and other taxes and fees, if any, payable to any governmental agency** in connection with the purchase and sale of Shares of AME and the consummation of the transactions contemplated herein x x x." *(Emphasis supplied)*

Hence, the respondent has neither legal nor factual basis to contend that the stock purchase transaction between petitioner and IMI necessarily entailed a sale of AME's assets for which the 10% VAT may be imposed.

Proceeding to the second issue.

Respondent claims that the communication *(Exhibit "OO")* sent by petitioner to T.L. Ltd., its foreign, non-resident customer, requesting the latter to course the inward remittance of its assembly fees through specified local banks with which

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petitioner maintains an account was in fact a bill of exchange or an order for the payment of money purporting to be drawn in a foreign country but payable in the Philippines subject to DST under Section 181 of the Tax Code of 1993. However, this is again baseless.

Section 181 of the Tax Code provides:

> "**Section 181. Stamp tax upon acceptance of bills of exchange and others.** – Upon any acceptance or payment of any bill of exchange or order for the payment of money purporting to be drawn in a foreign country but payable in the Philippines, there shall be collected a documentary stamp tax of thirty centavos on each Two hundred pesos or fractional part thereof, of the face value of any such bill of exchange, or order, or the Philippine equivalent of such value, if expressed in foreign currency."

Undeniably from the foregoing, the said provision does not apply to the communication transmitted by petitioner to its customer abroad. The same is simply an advice from petitioner to channel its customer's remittances to the designated banks where petitioner maintains a foreign currency account. Such written advice cannot be considered a bill of exchange, letter of credit, or any order for payment of money as they are understood in their commercial sense and under existing regulations and settled jurisprudence.

Under **Section 39 of Revenue Regulations No. 26**, otherwise known as the Revised Documentary Stamp Tax Regulations, the term "Bill of Exchange" denotes checks, drafts, and all other kinds of orders for the payment of money payable at sight or demand or after a specific period after sight or after a stated date. It is likewise defined as an open letter addressed by one person to another directing him, in effect, to pay, absolutely and at all events, a certain sum of money therein named, to a third person, or to any other to whom that third person may order it to be paid, or it may be payable to bearer or to the drawer himself *(Black's Law Dictionary, 1968 Edition).*

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On the other hand, an order for payment is defined as "something in the nature of a bill payable in money or something else, but in a more extensive sense, it includes a direction or request to pay over money or other things upon the credit of the drawer, although to be carried by the payee as the mere servant of the drawer to him or to be applied to his use" (**State vs. Nevina,** *23 Vt. 519, 21, cited in 31A Words and Phrases 176 [Perm Ed]*).

Unlike the disputed communiqué issued by petitioner, bills of exchange and orders for payment are initiated by the buyer. Bills of exchange are drawn by the buyer in payment of its obligations to the seller, while an order for payment, like bills of exchange, presupposes a situation where a buyer upon his credit requests a bank to pay the seller an amount of money for the purpose of discharging an obligation.

This is not true in the case of petitioner, which merely transmitted an instruction to T.L. Ltd. for the purpose only of specifying the banks where the latter will remit the foreign currency service/assembly fees. In other words, the situation merely involves two parties, namely, petitioner, as seller, and T.L. Ltd., which is not ordered to remit payments but is simply advised about its preference as to how exactly it should effect the remittance.

It is erroneous to interpret T.L. Ltd.'s remittances to the local banks designated by petitioner to mean payments to a third person as contemplated by bills of exchanges or as orders of payment. That respondent's contention deserves scant consideration is clearly seen from the fact that said remittances were not payment to the banks but merely a disposition of the funds to the said banks in accordance with the instructions of the seller (petitioner), the payee being the seller and not the bank.

The petitioner made no payment to T.L. Ltd. and vice versa. Since there was neither payment nor order of payment, the transaction cannot be subject to DST.

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Thus, the DST assessment's failure to meet this requirement leaves it bereft of any legal basis.

As regards the third issue, respondent assessed petitioner of deficiency withholding tax representing 5% of the rental payments of P832,720.24 made to Ms. Vilma Santos-Recto *(Exhibit 7)* for 1994 which was retained by petitioner for its expatriates' employees. Respondent's investigation revealed that petitioner failed to subject said rental payments to 5% expanded withholding tax pursuant to Section 1(c) of Revenue Regulation No. 5-82. The basis of respondent for such assessment was the unofficial receipt issued by Ms. Santos showing receipt of payment in the sum of P832,720.24. Respondent's computation of deficiency expanded withholding tax *(Exhibit BBB)* is detailed as follows:

Total rental payments	P832,720.24
Expanded withholding tax rate [per Rev. Reg. # 5-82, Sec. 1(C)]	5%
Total Tax Due	P 41,636.01
Surcharge	10,409.00
Interest	31,227.01
Compromise	5,000.00
Total EWT deficiency	P 88,272.02

Petitioner objected to the factual accuracy of the assessment because according to it the withholding tax return and the accompanying alpha list *(Exhibits C-1 and C-2)* show that it paid the expanded withholding tax on the said rentals in the amount of P45,000.00 for the total rental payments amounting to P900,000.00 as expressly stated in the Contract of Lease *(Exhibit C)*.

Petitioner's objection is untenable.

Exhibits C-1 and C-2 cited by petitioner show that the amount of tax withheld involves rental payments made in 1995. Inasmuch as the assessment covers taxable

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year 1994 and petitioner failed to refute the same, respondent's inclusion of this item in the computation of the deficiency withholding tax is proper.

Anent the fourth issue, petitioner extended income benefits to its expatriate employees in the year 1994 which include tuition fees paid by petitioner for the dependents of the expatriates and the housing and lodging given to the expatriates and their families. On the basis of the aforementioned benefits, respondent assessed petitioner for deficiency withholding tax on account of petitioner's failure to withhold the tax due therefrom pursuant to Sec. 22 (b) of the National Internal Revenue Code, which provides:

> "**Section 22.** ***Tax on nonresident alien individual.*** –
>
> **(b) Nonresident alien not engaged in trade or business within the Philippines. –** There shall be levied, collected and paid for each taxable year upon the entire income received from all sources within the Philippines by every nonresident alien individual not engaged in trade or business within the Philippines as interest, dividends, rents, salaries, wages, premiums, annuities, compensation, remuneration, emoluments, or other fixed or determinable annual or periodical or casual gains, profits, and income, and capital gains (except capital gains realized from buying and/or selling shares of stock xxx), a tax equal to 30% of such income xxx."

The deficiency withholding taxes were computed by respondent as follows:

a. Tuition fees paid by petitioner for the dependents of the expatriates:

Jan. (USD27,043.50 at P28.00)	P 757,218.00
July (USD25,863.85 at P26.50)	685,392.03
August (USD7,000 at P26.50)	185,500.00
Oct (USD335.00at P26.50)	8,542.50
Total	**P 1,636,652.53**
Tax Rate [Sec. 22(b) NIRC]	30%
Tax Due	**P 490,995.76**
Surcharge	122,748.94
Interest	368,246.82
Compromise	20,000.00
Total tax still due	**P 1,001,991.52**

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b. Housing and lodging given to the expatriates and their families

Total rental	P	832,720.24
Tax rate (Sec. 22(b) NIRC)		30%
Tax Due	**P**	**249,816.07**
Surcharge		62,454.02
Interest		187,362.05
Compromise		15,000.00
Total tax still due	**P**	**514,632.14**

Petitioner disagreed with respondent stating that:

> "With regard to the tuition fees paid to the dependents of the expatriates, Petitioner respectfully submits that even granting no tax was withheld from the income benefits, it is of record that the beneficiaries themselves (Petitioner's expatriates) declared the amount thereof as part of their gross income in their individual income tax returns and have paid the necessary income taxes due thereon.
>
> With regard to the housing and lodging benefits, the records likewise disclose that the individual expatriates declared 50% of the value of the benefits in their individual income tax returns and paid the necessary income taxes thereon pursuant to the provisions of **Revenue Audit Memorandum Order 1-87.**"

Respondent's assessment is meritorious. The individual income tax returns referred to by petitioner were not presented for verification by this court. And even if such individual income tax returns were offered in evidence, the assessment will still prosper because the assessment was based on petitioner's obligation to withhold and remit tax as the withholding agent of the Government. Its failure to withhold and remit has the consequence of paying the tax under Section 51 in relation with Section 251 of the National Internal Revenue Code of 1977 (**Commissioner of Internal Revenue vs. The Court of Appeals, Court of Tax Appeals and A. Soriano Corp.**, *GR. No. 108576, January 20, 1999)*.

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We now resolve the issues of whether petitioner withheld and remitted the tax on interest payment it made on its loan from Advance Micro Devices, Inc. and whether the proper tax rate to be used is 15% pursuant to the RP-US Tax Treaty or 20% pursuant to the Tax Code.

The pieces of evidence on record confirmed the averment that petitioner withheld and remitted the 15% tax on interest payment on its loan from Advance Micro Devices, Inc. (AMD), as evidenced by the "Management of External Debt Department (MEDD) Ref No. A034468" issued by the Bangko Sentral ng Pilipinas *(Exhibit" TT")*. This is further supported by other evidence showing the remittance and payment made by petitioner to AMD as approved by the Management of the External Debt Department of the Bangko Sentral ng Pilipinas *(Exhibits TT and LL)*, BSP letters of approval of remittance stating the 15% withholding tax and the pertinent withholding tax returns *(Exhibits E to P, R to Z and AA to FF)* with the corresponding summary of monthly remittances *(Exhibits UU and VV)* showing the withholding of tax at the rate of 15%.

What remains unsettled is the question on the proper tax rate to be used for such interest payment made by petitioner. Should it be the 15% tax rate pursuant to the RP-US Tax Treaty or the 20% imposed by the 1977 National Internal Revenue Code (NIRC)?

Respondent believes that the tax rate should be 20% and not 15% basing his legal support on Section 25 (b)(5) of the NIRC which provides:

> **"Section 25. *Rates of tax on foreign corporation.* –**
>
> **(b) Nonresident foreign corporation. –**
>
> **(5) Tax on certain incomes received by nonresident foreign corporation.** – (A) Interest on foreign loans contracted on or after August 1, 1986 shall be subject to a 20% tax."

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Meanwhile, petitioner contends that the applicable withholding tax rate for its interest payments to AMD must only be 15% pursuant to Article 12 (2) of the RP-US Tax Treaty which provides that the "Interest derived by a resident of one of the Contracting States from sources within the other Contracting State shall not be taxed by the other Contracting State at a rate in excess of 15 percent of the gross amount of such interest."

The Court agrees with petitioner.

In a refund case of **Benpres Holdings Corporation versus Commissioner of Internal Revenue**, *CTA Case No. 6010, January 2, 2001,* where the sole issue raised was whether the interest payments made by the petitioner should be taxed at the rate of 20% based on BIR Ruling 52-98 or at 10% as provided by the RP-US Tax Treaty, this Court held that petitioner Benpres is liable only to pay tax at the rate of 10%.

Noteworthy is the fact that the tax treaty that was entered into between the Republic of the Philippines and the United States of America is a valid limitation on the sovereignty of both states. Hence, the municipal law which in this case is the 1977 National Internal Revenue Code of the Philippines will yield to the validly entered tax treaty. Accordingly, the applicable tax rate on the interest payment made by petitioner to Advanced Micro Devices is 15%.

We now proceed to the sixth issue.

Respondent assessed petitioner for expanded withholding tax on petitioner's payment of shuttle service fees to PJC Bus Service for the service of the latter in providing transport/shuttle services in favor of petitioner's employees from their area of residence to petitioner's workplace *(Par. 9, Joint Stipulation of facts and Issues)*.

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Petitioner argues that its payment of the shuttle services fees are not subject to EWT since persons or entities engaged in the carriage of persons or passengers are not among those specifically enumerated in Revenue Regulations No. 6-85, as amended.

A review of the amendments to said regulations confirms this limitation that only transportation contractors for the carriage of goods are subject to the 1% EWT. Revenue Regulations No. 6-85 is hereunder quoted for easy reference, thus:

> "Section 1(e)2(e) of Revenue Regulations No. 6-85 is hereby amended to read as follows:
>
> "(e) Transportation contractors, which include common carriers, **for the carriage of goods and merchandise of whatever kind** by land, air or water, provided that the freight payment for such shipment is five thousand pesos (P5,000.00) or more." xxx" *(Emphasis supplied)*

Evidently, the above-quoted regulation specifically excludes transportation contractors or common carriers of persons or passengers. Accordingly, the assessment on petitioner's payment of shuttle service fees must be cancelled.

Likewise, respondent asserts that petitioner's payments to its medical doctors who render medical services to its employees should be subject to the 1% EWT pursuant to Revenue Regulations No. 12-94. Respondent computed the assessment as follows:

Total (Excluding Sept.)	P 9,614,998.36
Averaging (for Sept.)	
(P9,614,998.36/11 mos.)	874,090.76
Total	P10,489,089.12
Expanded Withholding Tax Rate *[RR# 12-94 (N)]*	1%
Tax Due	P 104,890.89
Surcharge	26,222.72
Interest	78,668.17
Compromise	10,000.00
Total Expanded Withholding Tax Deficiency	P 219,781.78

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Petitioner counters that it withheld the 10% tax on professional payments to the medical doctors who rendered medical services to its employees. As proof of its retention, petitioner presented its Annual Information Return of Creditable Income Tax Withheld for 1994 *(Exhibit QQ)* and the corresponding Alpha List I *(Exhibit QQ-1)* to show that it withheld payments made to the medical practitioners.

After a judicious study of the records of this case, the Court verified that indeed petitioner withheld 10% tax on income payments made to its medical doctors. Thus, the assessment of this item is cancelled.

With respect to the seventh issue, as a backgrounder, petitioner entered into an agreement with Copper Kettle on March 26, 1991, wherein the latter would operate a canteen within the company premises and cater to the meal requirements of petitioner's personnel *(Paragraph 8, Joint Stipulation of Facts and Issues)*. In lieu of providing cash meal subsidies to its employees as part of their benefits, petitioner instead distributed meal tickets or coupons *(Exhibit "PP")* to the individual employees every payday, which they presented to copper Kettle in payment of their meals. These meal tickets are of relatively small value and were provided by petitioner to insure that the personnel are available anytime and would no longer have to leave the company premises just to have their meals taken outside.

The agreement with Copper Kettle provides, among others, that it shall collect from petitioner the cash value of the meal tickets or coupons within a maximum period of fifteen (15) days after submission of said tickets and that petitioner shall bear all the expenses for gas, water and electricity incident to Copper Kettle's operation of the canteen within company premises.

From the foregoing, it is apparent that the amounts paid by petitioner do not represent fees for services rendered by Copper Kettle. They are simply the cash

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equivalent of meal tickets presented by the employees upon every meal consumed by petitioner's employees, while the "economic benefits", i.e., expenses for gas, water and electricity incident to Copper Kettle's operations are in fact for the benefit of the petitioner and not for Copper Kettle.

We now tackle the issue of tax rate of interest payments on public issuances of Floating Rate Notes.

As a factual backdrop, petitioner issued Guaranteed Floating Rate Notes (GFRNs) in 1994 in the total amount of $14,000,000.00 and in denominations of US$500,000.00 each, which were set to mature on February of 2000 *(Paragraph 11, Joint Stipulation of facts and Issues)*.

The GFRNs issued by the petitioner constitute a direct and unconditional obligation of petitioner in the form of notes payable to bearer. Petitioner is obligated to pay interest on the GFRN semi-annually which is the sum of 6% per annum and the London Interbank Offered Rate (LIBOR) for six-month US dollar deposits. The payment of interest shall continue until the note's redemption by the issuer, which is the petitioner.

Plainly, the GFRNs are instruments of debt and for being sold or floated outside the Philippines partake the nature of a foreign loan. The claim that the GFRN must be considered as a registered foreign loan is further shown by the fact that it was previously evaluated and approved by the Bangko Sentral ng Pilipinas (BSP). Hence, after petitioner's application, the BSP through its External Debt Department, issued a letter dated July 18, 1994 *(Exhibit "B-3", Reference No. 8-031215)* approving petitioner's application to issue the GFRNs. Consequently, the interest paid thereon by petitioner is subject to the provision of Section 25(b)(5)(A) of the Tax Code of 1993, save only when any particular tax treaty applies.

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In this regard, it must be pointed out that respondent has previously and categorically ruled that interests payments on the public issuance of floating rate notes are subject to the general preferential Tax Treaty rate of 10%. BIR Ruling UN-365-94 dated December 22, 1994 *(Exhibit "B-6")*, reads in part as follows:

> **"xxx You now request in behalf of your client, Dae Ryung, for confirmation of your opinion that the interest it will pay on its public issuance of floating rate notes is subject to the tax treaty rate of 10%.**
>
> **In reply, please be informed that your opinion is hereby confirmed. The withholding tax rates on interest payments to purchasers of publicly issued floating rates notes sold to residents of tax treaty countries** such as the United States, Unite Kingdom, Australia, Austria, Belgium, Brazil, Canada, Finland, France, Indonesia, Italy, Korea, Netherlands, New Zealand, Pakistan, Singapore and Thailand **is 10% of the gross amount.** [Art. 12(3) RP-US Tax Treaty; Art. 10(3) RP-UK Tax Treaty; Art. 11(8) RP-Australia Tax Treaty; Art. 11(2)(a) RP-Austria; Art. 11(3)(c) RP-Belgium Tax Treaty; Art. 11(3)(c) RP-Brazil Tax Treaty; Art. 11(7)(d) RP-Canada Tax treaty; Art. 11(7)(d) RP-Finland Tax Treaty; Art. 11(3)(c) RP-France Tax treaty; Art. 11(3)(b) RP-Indonesia Tax Treaty; Art. 11(2) RP-Italy Tax Treaty; Art. 11(2)(a) RP-Korea Tax Treaty; Art. 11(20)(a) RP-Netherlands Tax Treaty; Art. 11(8) RP-New Zealand; Art. 11(7)(b) RP-Pakistan; Art. 11(7)(b) RP-Singapore; and Art. 12(2)(a)(ii) RP-Thailand.] xxx"

Accordingly, the publicly issued GFRNs are debt instruments and the interest due thereon are subject to the provisions of Section 25(b)(5)(A) of the Tax Code of 1993, or as explained above is subject to applicable tax treaties entered into by the Philippines with other countries.

Regarding the issue of professional fees paid by petitioner to its legal retainer Bito, Lozada, Ortega and Castillo Law Offices (Bito Lozada Law Office) as actually intended for and paid to a non-resident legal retainer of petitioner, the Court again rules against the respondent's findings.

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According to respondent, during the conduct of its investigation, it was found out that petitioner credited Account No. 10728345 c/o Citibank N.A. International Banking Center, 399 Park Ave., New York, USA the amount of USD105,000.00 (P2,800,000.00) which led the examiner to believe that the account was a foreign-owned account because petitioner could not say who owns the said account to which it credited the amount in question. And since petitioner failed to substantiate its claim that the said amount was paid to Bito Lozada Law Office, respondent assessed petitioner under Section 25(b)(1) of the National Internal Revenue Code of 1977.

Petitioner maintains that the finding is purely conjecture and has no factual basis. It asserts that petitioner paid legal fees to Bito Lozada Law Office in 1994 for various services rendered by the latter from May 18, 1993 to December 2, 1993, in connection with the purchase by petitioner of Automated Micro Electronics, Inc. in 1993. Bito Lozada Law Office billed petitioner as stated in Bill No. 10019 *(Exhibit D)* the amount of US$100,000.00 for the said legal services, for which petitioner paid the same amount in US dollars. Said billing was paid for in US dollars in view of the fact that the law office's billing was quoted in US dollars.

Petitioner declares that pursuant to said bill, it applied for a Telegraphic Fund Transfer with PCI Bank requesting the bank to pay $100,000.00 to Bito Lozada Law Office's account in Citibank, New York. The Telegraphic Fund Transfer *(Exhibit D-4)* presented by the petitioner shows that such an amount was credited to the beneficiary, Bito Lozada Ortega & Castillo Law Office through its account (Account No. 10728345) with Citibank N.A. of International Banking Center, 399 Park Avenue, New York.

Based on a thorough study of the records of this case, the Court determined the existence of the following:

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- On March 3, 1994, the firm Bito, Lozada, Ortega & Castillo, as certified true and correct by the member of the firm named Gregorio F. Ortega, billed petitioner the amount of US$100,000.00 *(Exhibit D-1)* for the professional services it rendered to petitioner for the period beginning May 18, 1993 to December 2, 1993, as contained in Bill No. 10019 *(Exhibit D)*.

- Petitioner's journal voucher for the period ending April 24, 1994 (Exhibit D-2) showed the payment of legal fees in the amount of US$100,000.00 which contained an explanation as "various US Dollar disbursements during the month."

- A Telegraphic Transfer *(Exhibit D-4)* to the beneficiary Bito Lozada Ortega & Castillo in the amount of US$100,000.00.

It is thus clear that the payment of the professional fees was indeed made to Bito Lozada, and not to petitioner's alleged non-resident legal retainer. The assessment therefore should be cancelled.

As to the tenth issue, respondent theorizes that petitioner obtained a loan from the Bank of the Philippine Islands (BPI) in the amount of US$5,000,000.00 which petitioner failed to pay the corresponding documentary stamp tax due thereon which became the basis of respondent imputation of DST. Respondent computed the assessment as follows:

Conversion	
(USD5,000,000.00 at P28.00)	P140,000,000.00
Documentary Stamp Tax	
(Sec. 180 NIRC/RMC no. 4-94)	/200 x P0.30
Tax Due	P 210,000.00
Surcharge	52,500.00
Total Tax Still Due	P 262,500.00

Petitioner objects to respondent's accusation of non-payment of DST due on the loan obtained from BPI because BPI supposedly withheld the imposable DST on the transaction pursuant to Section 180 of the Tax Code.

Unfortunately, petitioner's objection holds no water. The Court could not find any documentary evidence that would support petitioner's allegation that indeed BPI had already withheld the DST due. Thus, respondent's assessment of this item should be upheld.

We will now settle the eleventh issue.

Respondent claims that the DST rate applicable in the issuance of preferred shares to Integrated Micro Electronics, Inc. (IMI) in connection with its sale to petitioner of all its interest in Automated Micro Electronics (AME) for the amount of P130,000,000.00 is P2.00 on each P200.00 of par value based on the provisions of Republic Act No. 7660. On this premise, respondent made the following assessment based on the original issuance of preferred shares, to wit:

Number of preferred shares issued	3,446,476
Par value	P1.00/share
Total preferred stock issued	P3,446,476.00
Documentary Stamp Tax rate (Sec. 175, NIRC-Original issue, RMC no. 4-94)	200xP2.00
Tax Due	P 34,466.00
Surcharge	8,616.50
Total Tax still due	P 43,082.50

Petitioner reasons that it paid DST on the original issuance of preferred shares at the rate of P1.70 for every P200.00 of the total par value, which is the correct rate at the time the transaction was made.

After a judicious scrutiny of the records, it is determined that on December 2, 1993, petitioner made two issuances of its preferred stock for Integrated Micro Electronics, Inc. (IMI) for the total shares of 3,446,476 *(Exhibit XX)* of which the documentary stamp tax of P29,326.60 was paid thereto on January 11, 1994 *(Exhibits WW and WWW)*. The first issuance involved 3,434,306 preferred shares while the second issuance involved 12,170 shares *(Exhibits EEE and XX)*. On the same date,

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the 12,170 preferred shares holding of IMI was cancelled and transferred to International Finance Corporation *(Exhibits XX and XX-1)*.

On November 9, 1994 records revealed that petitioner subsequently issued 12,170 preferred shares to IMI *(Exhibits FFF and XX)* but there was no evidence which would show that the preferred shares issued was subjected to DST. So, the total issued and outstanding preferred shares of stock held by IMI as of November 9, 1994 was 3,446,476 shares.

Therefore, the rate applicable is P1.70 per P200.00 for the first two issuances made on December 2, 1993 and P2.00 per P200.00 for the third issuance made on November 9, 1994. It follows that respondent's assessment should be upheld with respect to the issuance made on November 9, 1994 at the rate of P2.00 per P200.00 of the total par value of the preferred stock issued amounting to P121.70 plus surcharge of P30.43 or a total amount of P152.13 as deficiency DST.

Relative to the twelfth issue, in order to properly resolve this question, a review of the subject transaction is appropriate.

In 1989, Advanced Micro Devices (AMD) sold its 46,700,000 common shares in petitioner to T.L. Ltd., as shown by the agreement of purchase and Sale of Stock between AMD and T.L.Ltd. *(Exhibit "ZZ")*. Petitioner assumed the payment of the DST on this transfer in the amount of P116,750.00 as evidenced by the confirmation receipt (No. B16022485), dated April 26, 1989 and Certification of Payment, dated June 7, 2000.

Based on the above recitation of events, it is apparent that the transaction in question did not involve original issuance of shares but a mere transfer or sale of shares which is subject to DST under Section 176 of the Tax Code of 1993.

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Section 176 of the Tax Code of 1993 provides that:

> "**Section 176. Stamp Tax on Sale, Agreements to Sell, Memoranda of Sales, Deliveries or Transfer of Due-bills, Certificates of Obligation, or Shares or Certificates of Stock.** – On all sales, or agreements to sell, or memoranda of sale, or deliveries, or transfer of due-bills, certificates of obligation, or shares or certificates of stock in any association, company or corporation, x x x there shall be collected a documentary stamp tax of One peso (P1.00) on each two hundred pesos, or fractional part thereof, of the par value of such due-bill, certificates of obligation or stock: x x x"

In view of the foregoing, the Court finds that the assessment of DST for original issuance of shares is clearly erroneous and without legal basis.

Delving now on the thirteenth issue, respondent contends that the Supply Agreement entered into by petitioner and T. L. Limited *(Exhibit MM)* is a Royalty Agreement, whereby, for a consideration paid to T. L. Ltd., petitioner acquired technical know-how in its assembly, testing, and manufacture of electronic components. Respondent interpreted petitioner's income from T. L. Limited as gross income from which the basis for a royalty fee could be made. Respondent computed the assessment as follows:

Central Bank Circular no. 393 - Technical Service	
Total Assembly fee	P 1,758,746,913.00
Rate (CB Circular no. 393)	3%
Balance (Income payments to non-resident alien)	P 52,762,407.39
Tax Rate	30%
Total tax still due on the Income payment	P 15,828,722.22
Surcharge	3,957,180.00
Interest	11,871,541.66
Compromise	25,000.00
Total Tax Due	P 31,628,444.43

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Petitioner disputes that the questioned assembly fees as provided for by the Supply Agreement are not income payments but are in fact income received by petitioner for its services rendered to TL Limited.

Petitioner in its memorandum explained that it entered into a Supply Agreement with T. L. Limited *(Exhibit MM)* wherein petitioner shall assemble, test, and manufacture electronic components and parts using direct materials supplied by T. L. Limited on a consignment basis. Petitioner will then re-sell the finished product to T. L. Limited which is bound to pay petitioner a value-added amount based upon a predetermined standard cost, taking into consideration standard machine rates, labor, and overhead rates. According to petitioner this fact is clearly shown in Articles 1.1 and 1.2 of the Supply Agreement *(Exhibit MM)* between petitioner and T. L. Limited, which provide:

> "1.1 AAPI shall assemble, test and/or manufacture electronic components and parts according to instructions and orders issued from time to time by TLL.
>
> 1.2 TLL shall supply, or cause to be supplied, all direct materials required to fulfill such orders as it from time to time places with AAPI."

Petitioner further explains that the agreement is not a royalty agreement as contemplated by respondent, since petitioner is not bound under any royalty agreement to remit to T. L. Limited royalties or other form of consideration for the use or transfer of technology.

Thus, petitioner concludes that there is clearly no basis for respondent to assume that it made such payments to a non-resident payee and impute alleged unpaid income or withholding tax thereon when it was petitioner which actually received income in the amount of P1,758,746,913.00 *(Exhibit NN-1)* as shown in petitioner's Financial Statements *(Exhibit NN)*.

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Indeed, after a careful examination of the documents presented, the Court verified that the amount of P1,758,746,913.00 actually represents "Assembly Fee" as reflected in petitioner's financial statement and not payment of royalty. Therefore, respondent's assessment of this item is devoid of merit.

Finally with regard to the fourteenth issue, respondent alleges that petitioner entered into several transactions, which were subject to income tax and/or DST, to wit:

1. Land transfer from Integrated Micro Electronics, Inc. (IMI) to IMI Realty Inc. (IRI) in payment of shares of stock:
2. Alleged "indirect" transfer of land from IRI to petitioner;
3. Alleged "indirect" transfer of building from IMI to petitioner; and
4. Alleged "indirect" transfer of land and building from petitioner to Salcedo Sunvar Realty.

A background of the transactions in question is appropriate.

In late 1993, Integrated Micro Electronics, Inc. (IMI) forged an agreement with IMI Realty, Inc. (IRI) whereby the former exchanged several parcels of land for the latter's shares of stock, which resulted in IMI gaining control of IRI. The BIR confirmed the transaction as a tax-free exchange in BIR Ruling No. 522-93 in accordance with then Section 36(c)(2)(c) of the Tax Code of 1978 *(Exhibit "CCC")*.

Subsequently, IMI, which is the registered owner of several buildings as well as the holder of 100% of the equity of IRI due to the tax-free exchange, entered into separate agreements with Salcedo Sunvar Realty, Inc. (Sunvar) for the sale of said buildings and IRI shares. Sunvar is a domestic company, 40% of the capital stock of which is owned by petitioner, as shown by the Articles of Incorporation *(Exhibit*

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"DDD and DDD-1") of Salcedo Sunvar Realty. Petitioner loaned to Sunvar the amount required to purchase the said buildings and shares from IMI.

Respondent avers that the sale of shares of IRI from IMI to Sunvar should be construed and treated for income tax purposes as an "indirect" transfer of IRI's land to petitioner, which should be liable for both income tax and DST on the transaction. Likewise, respondent concludes that the sale of the building from IMI to Sunvar should be treated for tax purposes as an "indirect" transfer to petitioner as well.

However, respondent's findings have no basis in fact and law.

First of all, the petitioner has no liability for the alleged withholding tax and DST due on the transfer by IMI of land to IRI because **petitioner was not in any manner privy to the transaction.** Thus, it is a matter that the BIR must pursue against the concerned parties.

Second, respondent's allegation that there was an "indirect" transfer of land from IRI to petitioner on the premise alone that petitioner holds 40% of the equity of Sunvar is totally baseless and unsupported by any credible evidence.

The basic doctrine of corporate entity is that a corporation has a personality distinct and separate from its stockholders. The stockholders or members compose the corporation but they are not the corporation. A corporation is a legal or juridical person with a personality separate and apart from its individual members or stockholders *(Hector De Leon, The Corporation Code, p. 16).* Having such distinct personality, it may own property, real or personal, under its own name. Property conveyed to or acquired by the corporation is in law the property of the corporation itself as a distinct legal entity and not that of the stockholders or members as such *(Hector De Leon, The Corporation Code, supra, Article 44, Civil Code).*

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In other words, if IRI owns the property under its own name, and Sunvar, which is a stockholder of IRI due to the sale of the IRI shares from IMI, cannot claim ownership over the property of the corporation, then with more reason is petitioner, which is a mere stockholder of Sunvar.

In **Creese vs. Court of Appeals,** *93 SCRA 483*, the Supreme Court held that the corporation may not, generally, be made to answer for acts or liabilities of its stockholders or members or those of the legal entities to which it may be connected and vice versa.

Again, the Court reiterates that Sunvar has a separate and distinct personality from the petitioner, as evidenced by Sunvar's Articles of Incorporation *(Exhibit "DDD")*. The assessment actually attempted to pierce the corporate veil by disregarding the fiction of corporate entity and seeing the corporation and the stockholders as one. Yet, in his zealousness to do so, respondent has patently disregarded settled jurisprudence and the court's basic rules.

The doctrine of "piercing the veil of Corporate fiction" is not applicable to the case at bar. The general rule is that a corporation, being a mere creature of the law, may be allowed to exist solely for lawful purposes; but where the fiction of corporate entity is being used as a cloak or cover for fraud or illegality, or to defeat convenience, justify wrong, protect fraud, or defend crime or for ends subversive of the policy and purpose behind its creation, especially where the corporation is a closed family corporation, this fiction will be disregarded and the individuals composing it will be treated as identical. (**Claparols vs. Court of Industrial Relations**, *65 SCRA 613*; **Yutivo Sons Hardware Co. vs. Court of Tax Appeals**, *1 SCRA 160*; **Emiliano Cano Enterprise, Inc. vs. Court of Industrial Relations**, *13 SCRA 290*)

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Using this principle and jurisprudence as a yardstick, the question now is: Was respondent able to prove that petitioner in the transfer of lands used the veil of corporate fiction between and among separate corporate entities to defraud the government of taxes? The answer is in the negative.

The Court cannot understand why the revenue examiner suggested that petitioner tried to circumvent the law and evade taxes by organizing Sunvar as it itself could not own real property in the Philippines. This allegation is plainly speculative as there is nothing in the law which bars petitioner from making such investment in a realty company when all that the law requires is that a realty company must be at least 60% Filipino-owned *(Section 2, Article XII, Philippine Constitution)*.

As correctly pointed out by the petitioner, while it is true that revenue officers, in proper cases, may disregard the separate corporate entity where it serves as a shield for tax evasion (**Commissioner of Internal Revenue vs. Norton Harrison Company**, *G.R. no. L-17618, August 31, 1964*), it is equally true that allegations of fraud, which is a serious charge, must be supported by clear and convincing evidence. And, where it is lacking, such allegations of fraud must be dismissed. (**Commissioner of Internal Revenue vs. Javier, et.al.,** *G.R. No. 78953, July 31, 1991*; **CIR vs. Yusay, et. al.** *G.R. No. L-19495, November 24, 1966*; **Collector of Internal Revenue vs. Benipayo**, *G.R. no. L-13656, January 31, 1962*)

In the case at bar, respondent presented absolutely no evidence to prove that Sunvar was set up to evade the payment of taxes on the transfers of property. On the other hand, petitioner managed to prove that Sunvar has a personality separate and distinct from petitioner *(Exhibits "DDD" and "DDD-1")*. Fraud and bad faith cannot be deduced from such transaction merely because petitioner is a stockholder in

Sunvar. Undoubtedly, respondent's claim of fraud and attempt to pierce the corporate veil of Sunvar must necessarily fail.

Now regarding the issue of the purported indirect transfer of land and building from petitioner to Salcedo Sunvar Realty, there are no facts, documents, or even the slightest evidence adduced to suggest and prove that petitioner sold land and building to Sunvar. What respondent, through the revenue examiner attempted to do, was to create different taxable events out of entirely the same transaction and seeking to tax petitioner in either, any or all of the situations. Hence, the ~~assessment has~~ absolutely no leg to stand on.

P10,452,417.75

WHEREFORE, the Court hereby cancels the assessment for deficiency value-added tax in the amount of ~~211,816,184.20~~ and upholds the assessments for deficiency withholding taxes and deficiency DST in the reduced amounts of **P1,564,895.68 and P262,652.13,** respectively, computed as follows:

Deficiency Withholding Tax

	Rental	Income Benefits	Total
Tax Base	P 832,720.24		
Tuition Fee		P 1,636,652.53	
Housing and Lodging		832,720.24	
Total Tax Base	P 832,720.24	P 2,469,372.77	
Multiply by Tax Rate	5%	30%	
Basic Deficiency Withholding Tax Due	P 41,636.01	P 740,811.83	P 782,447.84
Surcharge	10,409.00	185,202.96	195,611.96
Interest	31,227.01	555,608.87	586,835.88
Total Deficiency Withholding Tax Due	P 83,272.02	P 1,481,623.66	**P 1,564,895.68**

Deficiency Documentary Stamp Tax

	BPI Loan	Issuance of Preferred Stock to IMI	Total
Tax Base	P 140,000,000.00	P 12,170.00	
Multiply by Tax Rate	P0.30/P200.00	P2.00/P200.00	
Tax Due	P 210,000.00	P 121.70	P 210,121.70
Surcharge	52,500.00	30.43	52,530.43
Deficiency DST	P 262,500.00	P 152.13	**P 262,652.13**

Petitioner is likewise ordered to pay 20% delinquency interest from February 6, 1999 until full payment thereof pursuant to Section 249 (c) (3) of the 1993 Tax Code.

The Court cannot sustain respondent's imposition of compromise penalty since there was no compromise agreement reached by the parties (**Atlas Consolidated Mining and Development Corporation (doing business under the name of Atlas Itochu Consortium) vs. Commissioner of Internal Revenue,** *CTA Case No. 5671, promulgated on August 29, 2002*).

SO ORDERED.

ERNESTO D. ACOSTA
Presiding Justice

We concur:

LOVELL R. BAUTISTA
Associate Justice

CAESAR A. CASANOVA
Associate Justice

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