REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

MERALCO EMPLOYEES SAVINGS & LOAN ASSOCIATION, INC.,
Petitioner,

- versus -

C.T.A. CASE NO. 5564

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:
OCT 18 2000

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DECISION

This case emanated from a demand letter and assessments issued against Petitioner for deficiency withholding taxes covering the period 1988 and 1989 in the total amount of P4,155,067.73.

Petitioner is a private non-stock corporation duly registered with the Securities and Exchange Commission (Exh. A). It is principally organized to foster, promote and cultivate the habit of thrift and savings among its members (Exh. A-1).

On November 25, 1991, Petitioner received a demand letter from the Respondent for the payment of alleged deficiency withholding taxes in the total sum of P4,155,107.71 for the calendar years 1988 and 1989 (Exhs. OO/7), computed as follows:

(Assessment No. FAS-1-88-91-0033178 - Exhs. PP/1)
1988 Deficiency 5% Final Withholding
Taxes on Dividends Paid -

Deficiency basic 5% final withholding tax	P1,926,585.97
25% Surcharge	481,646.49
20% Interest per annum	1,669,929.58
Compromise penalty	50,000.00
TOTAL AMOUNT DUE AND COLLECTIBLE	P4,128,162.04

(FAS-1-88-91-0033179 - Exhs. QQ/2)
1988 Deficiency Expanded Withholding Tax -

Deficiency basic expanded withholding tax	P 3,376.61
25% Surcharge	844.15
20% Interest per annum	2,367.67
Compromise penalty	1,000.00
TOTAL AMOUNT DUE AND COLLECTIBLE	P 7,588.43

(FAS-1-88-91-0033180 - Exhs. RR/3)
1988 Compromise Penalties -

Non-submission of BIR Form 1701-B	P 1,000.00	
Non-submission of BIR Form 1743-B	1,000.00	
TOTAL AMOUNT DUE AND COLLECTIBLE	P 2,000.00	
TOTAL DEFICIENCY TAX FOR 1988		P4,137,750.47

(FAS-1-00-91-0033181 - Exhs. SS/4)
1989 Deficiency Expanded Withholding Tax -

Deficiency basic expanded withholding tax	P 6,382.50
25% Surcharge	1,595.60
20% Interest per annum	3,614.00
Compromise penalty	3,400.00
TOTAL AMOUNT DUE AND COLLECTIBLE	P 14,992.10

(FAS-1-88-91-0033182 - Exhs. TT/5)
1989 Deficiency Withholding Tax on Compensation -

Deficiency basic withholding tax on compensation (January 1989)	P 564.00
25% Surcharge	141.00
20% Interest per annum	383.72
Compromise penalty	400.00
TOTAL AMOUNT DUE AND COLLECTIBLE	P 1,488.72

(FAS-1-88-91-0033183 - Exhs. UU/6)
1989 Compromise Penalties for Late Remittance - of Expanded Withholding Tax (March 1989)

25% Surcharge	P 155.62
20% Interest per annum	80.80
Compromise for late filing	200.00
Compromise for late payment	400.00
TOTAL AMOUNT DUE AND COLLECTIBLE	P 836.42

TOTAL DEFICIENCY TAX FOR 1989	P 17,317.24
TOTAL DEFICIENCY TAXES FOR 1988 & 1989	P4,155,067.73

Consequently, Petitioner filed a written protest with the Bureau of Internal Revenue on December 3, 1991 questioning the subject assessments (Exh. VV).

On October 13, 1997, Petitioner received a letter from the Respondent dated January 28, 1997, denying its "request for reconsideration" with finality (Exh. WW).

Petitioner then came to this Court on November 12, 1997 by way of a Petition for Review to annul the said assessments for being arbitrary, oppressive, null and void and without any legal force and effect.

Petitioner alleged that the right of the Respondent to collect the subject assessments has already prescribed inasmuch as Petitioner's income tax returns were filed in 1989 and 1990 and the assessment notices were served upon the Petitioner on November 25, 1991.

Petitioner also avers that the subject "cash dividends" distributed to its members do not constitute and are outside the scope of the "cash dividend" contemplated under Section 21(c)(2) of the Tax Code for the following reasons:

> (a) Petitioner is a non-stock and non-profit corporation and the income which it distributes to its members comes from the members themselves (consisting of interest paid by members on the loans extended by the petitioner);
>
> (b) The relationship between the petitioner and its members is that of a debtor and creditor and not that of a corporation and stockholders; hence, the contributions made by the members of the petitioner as a savings and loan association are in the nature of a deposit or loan, which are different from the equity or capital contributions of the stockholders in an ordinary corporation;
>
> (c) The "dividends" distributed by the petitioner to its members are not in the nature of corporate profits, unrestricted retained earnings, or income arising from activity conducted for profit contemplated under Section 43 of the Corporation Code which are taxable; and
>
> (d) Assuming that the "dividends" distributed by the petitioner to its members are taxable, the same are taxable not as "cash dividends" but as "interest income".

Respondent, in his Special and Affirmative Defenses, had this to say:

> (1) Petitioner's right to contest the subject assessment has prescribed;
>
> (2) Petitioner is, in fact and in law, a corporation and does not possess the characteristics peculiar to a banking institution;

(3) The income paid by petitioner to the members are dividends and not interest; and

(4) Assessments are prima facie correct and made in good faith. The taxpayer has the duty in proving otherwise.

To support its position, Petitioner presented witnesses and submitted numerous documents which include, among others, monthly remittance returns, BIR payment orders, Central Bank confirmation receipts and annual income tax returns.

Respondent, for his part, likewise presented witnesses and several documents in refutation of Petitioner's claim. However, both parties opted not to file their respective memorandum.

The issues for Our determination are as follows:

1) Whether or not the right of the Respondent to collect has already prescribed;

2) Whether or not the cash dividends distributed by the Petitioner to its members are subject to final withholding tax under Section 21(c)(2) of the Tax Code, as amended.

After a painstaking review of the facts, issues, arguments of the parties, applicable laws, rules and jurisprudence, We rule against the Petitioner.

Section 203 of the Tax Code, mandates, to wit:

SEC. 203. ***Period of limitation upon assessment and collection.*** - Except as provided in the succeeding section, internal revenue taxes shall be assessed within three years after the last day prescribed by law for the filing of the return, and no proceeding in court without assessment for collection of such taxes shall be begun after the expiration of such period: *Provided*, That in a case where a return is filed beyond the period prescribed by law, the three-year period shall be counted from the day the return was filed. For the purposes of this section, a return filed before the

> last day prescribed by law for the filing thereof shall be considered as filed on such last day.

Section 224 of the same Code, on the other hand, provides in part:

> **SEC. 224.** ***Suspension of running of statute.*** - The running of the statute of limitations provided in Sections 203 and 223 on the making of assessment and the beginning of distraint or levy or a proceeding in court for collection, in respect of any deficiency, shall be suspended for the period during which the Commissioner is prohibited from making the assessment or beginning distraint or levy or a proceeding in court and for sixty days thereafter; when the taxpayer requests for a re-investigation which is granted by the Commissioner; when the taxpayer cannot be located in the address given by him in the return filed upon which a tax is being assessed or collected.

A reading of the denial letter of the then Commissioner of Internal Revenue leads Us to no other conclusion than that the protest letter filed by the Petitioner on December 3, 1991 was considered as a request for reinvestigation or reconsideration. In fact, on February 10, 1992, the whole docket of the case with the protest letter was forwarded by the Assistant Commissioner for Collection to the Chief, VAT Division (p. 209. BIR rec.). And on March 2, 1992, the expediente of the case was forwarded from the VAT Division to the Legal Service of the Bureau (p. 211, BIR rec.). That the denial finally came out only in 1997 is a matter better addressed to the Respondent.

In sum, the time to collect the deficiency taxes against Petitioner was suspended. Settled is the rule that the prescriptive period provided by law to make a collection by distraint or levy or by a proceeding in court is interrupted once a taxpayer requests for reinvestigation or reconsideration of the assessment **(Commissioner of Internal Revenue vs. Wyeth Suaco Laboratories, Inc., G.R. No. 76281, September 30, 1991)**. In the case at bar, one thing is clear though, no action for collection by way of distraint or levy or judicial action was made before said denial. Thus, this only indicates that the protest letter was entertained as a request for reinvestigation or reconsideration by the Respondent. It was only on October 13, 1997 that the first notice was sent to herein Petitioner requiring it to settle its tax liability of P4,155,067.71, otherwise, proper remedies for collection thereof be resorted to by the government (p. 223, BIR rec.).

Anent the second issue, Petitioner argues that it possesses the characteristic peculiar to a banking institution in that it accepts deposits from its members as their capital contributions with the privilege of obtaining a loan therefrom. And that the income it made is in reality, a rebate or interest on capital deposits of the members and should not be construed as dividends. Petitioner further opines that under American law, dividends paid by savings and loan associations are commonly referred to as interest.

We do not agree.

Under the basic principle of statutory construction, resort to foreign law is only proper if we have no law, rule or regulation to that effect. Hence, the reliance made by Petitioner on an alleged American law is misplaced since we have our own tax laws as well as the corresponding rules and regulations implementing the same. It is clearly enunciated under BIR Ruling No. 115-87 that a non-stock savings and loan association is classified as a mutual savings bank which is exempt from income tax pursuant to Section 27(b) of the Tax Code.

For clarity, the rest of the provision of said ruling is hereunder quoted:

> "One of the powers of a non-stock savings and loan association is to allow members-depositors to participate in the profits of its savings and loan association on the basis of their deposits on the date dividends are declared (Sec. 5(e), Republic Act No. 3779, as amended).

> <u>From the foregoing provisions of the law and regulations, it seems clear that the profits of a non-stock savings and loan association distributed to its members-depositors are considered dividends. Such being the case, said dividends having been received by individuals from a domestic corporation are subject to a final tax at a rate of 15% in 1986; 10% effective January 1, 1987; 5% effective January 1, 1988; and 0% effective January 1, 1989</u> (Sec. 21(c)(2), Tax Code, as amended by Executive Order No. 37). (Underscoring supplied.)

With the advent of the above ruling, the argument of the Petitioner that its relationship with the members-depositors is one of debtor and creditor bears no further discussion. Although it is not superfluous to mention that Section 2-A of the General Banking Act substantially provides that "savings and loan association, among other entities, shall not be considered as a banking institution, albeit, the Monetary Board shall regulate the same".

Petitioner also contends that its income are more in the nature of rebates or "interests" on the loans taken out and which are paid for the costs of its operation unlike dividends, which are actually that part or portion of the profits of a corporation set aside, declared and ordered by the directors to be paid notably to the stockholders on demand or a fixed time.

Such ratiocination of Petitioner is devoid of merit.

Interest is defined as compensation allowed by law or fixed by the parties for the use of money, a compensation which is paid by the borrowers of money to lender for its use, and generally by a debtor to his creditor in recompense for his detention of the debt (Black's Law Dictionary, 6th Ed., p. 76). On the other hand, the term "dividend" both in the technical sense and its ordinary acceptation, is that part or portion of the profits of the enterprise which the corporation, by its governing agents, sets apart for ratable division among the holders of the capital stock (Phil. Law Dictionary, 3rd Ed., Moreno, pp. 280-

281.). It ordinarily means the profits of a corporation apportioned among shareholders (Black's Law Dictionary, 6th Ed., p. 74.). Income includes ordinary dividends and dividends are usually the product of earnings in some form.

Patently, Petitioner would like Us to believe that the income (dividends) it distributes to its members come from the members themselves consisting of interest paid by them on their respective loans. However, it is plainly set forth in Petitioner's by-laws that "the funds of the corporation shall be derived from membership fees, capital distributions, savings deposits, time deposits, interest on loans, interest from investments and any and all charges that may be collected from the members". In other words, Petitioner's so-called income is not derived from interests on loans alone.

In addition, Petitioner maintains that the "dividends" distributed to its members are not in the nature of corporate profits, unrestricted retained earnings or income arising from activity conducted for profit contemplated under Section 43 of the Corporation Code because as Petitioner insists, it is a non-stock non-profit corporation.

It must be emphasized at this point that the articles of incorporation and by-laws of the Petitioner specifically stated that it is a non-stock corporation. Never was it expressed that it is a non-profit organization. In fact, its by-laws explicitly provides that "the Board of Directors may declare dividends twice a year, specifically, in January and July, out of the earnings arising from the business of the Association during the sixth month period preceding the date of dividend declaration, but only after the required withdrawals reserve has been set up or maintained". This statement alone belied Petitioner's arguments. Moreover, Petitioner's statements of earnings and expenses for taxable years 1988 and 1989 disclosed that its earnings are from interests from loans and deposits in banks, service charges and fees. And the notes to the financial statements of the Petitioner reflect that it declared cash dividends to its members.

Petitioner also asseverates that BIR Ruling No. 115-87 was issued when Petitioner was no longer in the position to withhold taxes for the simple reason that it had already distributed the profits and no longer had any control over them.

Still, We are not convinced. Because this case involved the period 1988 and 1989 and the BIR already issued said ruling on April 24, 1987. In short, the questioned ruling was already in existence before the subject dividends were distributed to its members. Therefore, there was no obstacle to the withholding of proper taxes therefrom.

The legal basis for the imposition of the 5% final tax on the dividends distributed by Petitioner to its members is found in Section 21_(2) of the 1989 Tax Code, which provides, thus:

Section 21(c)(2) of the Tax Code

> "(c) Certain passive incomes. - A tax rate prescribed below is hereby imposed upon the amount of the following items of the gross income received by a citizen or resident alien from sources within the Philippines:
>
> x x x x x x x x x
>
> 2) Dividends received from a domestic corporation and the share of an individual partner in a partnership subject to tax under Section 24(a) at the rate of 15% in 1986; 10% effective January 1, 1987; 5% effective January 1, 1988; and 0% effective January 1, 1989."

Therefore, the assessment of the 5% withholding tax on Petitioner's dividends distribution is correct and in accordance with law.

Lastly, as regards Petitioner's other deficiency taxes, it is evident from the records that Petitioner indeed failed to remit the questioned taxes and although there was remittance for March 1989, the same was belatedly accomplished (BIR rec., pp. 17-133).

Moreover, the records show Petitioner failed to contest those other findings of the Respondent.

IN THE LIGHT OF ALL THE FOREGOING, the instant petition is hereby **DENIED** for lack of merit. The demand letter issued by the Respondent on November 7, 1997 and the accompanying assessment notices namely: Assessment Notice Nos. FAS-1-88-0033178, FAS-1-88-0033179, FAS-1-88-0033180, FAS-1-88-0033181, FAS-1-88-0033182 and FAS-1-88-0033183 are **UPHELD.**

Accordingly, Petitioner is **ORDERED** to **PAY** to the Respondent the amount of P4,155,107.71 representing deficiency withholding taxes for 1988 and 1989, plus interest accruing thereon until the time of full payment thereof.

SO ORDERED.

ERNESTO D. ACOSTA
Presiding Judge

WE CONCUR:

RAMON O. DE VEYRA
Associate Judge

AMANCIO Q. SAGA
Associate Judge

CERTIFICATION

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

ERNESTO D. ACOSTA
Presiding Judge