REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

FIRST DIVISION

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THE COCA-COLA EXPORT CORPORATION,
Petitioner,

- versus -

THE COMMISSIONER OF INTERNAL REVENUE,
Respondent.

C.T.A. CASE NO. 6861

Members:

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

Promulgated:

NOV 2 2 2005

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DECISION

ACOSTA, E., P.J.:

This is a judicial claim for refund or issuance of a tax credit certificate of the alleged erroneously withheld and remitted final withholding taxes on petitioner's royalty payments in the amount of **THIRTY SEVEN MILLION FIFTY FOUR THOUSAND FIVE HUNDRED SIXTY SEVEN AND 02/100 PESOS (P37,054,567.02)** covering the period January 2002 to June 2002.

The facts as stipulated by the parties are as follows:

Petitioner is a corporation organized and existing under the laws of the State of Delaware, United States of America (*par. 1, Joint Stipulation of Facts & Issues*). It is duly licensed and registered to do business in the Philippines through a Philippine branch, with its place of business at the 10th Floor, King's Court Building, 2129 Chino Roces Avenue, Makati City (*par. 2, Joint Stipulation of Facts & Issues*). Respondent, on the other hand, is the duly appointed Commissioner of Internal Revenue, who holds office at the BIR National Office

Building, located at Agham Road, Diliman, Quezon City (*par. 3, Joint Stipulation of Facts & Issues*).

Effective January 1, 2001, petitioner and The Coca-Cola Company (TCCC), a company not registered and licensed to do business here in the Philippines but is duly organized and existing under the laws of the State of Delaware, U.S.A., entered into a Royalty Agreement where petitioner agreed to pay TCCC a royalty fee for the use of certain trademarks, secret processes and formulae, and other confidential know-how as well as for the use of other intangibles relating to or in connection with the manufacture of concentrates beverage bases and syrups used in the preparation of certain beverages *(Exhibit "A")*. In this regard, the Philippine Intellectual Property Office issued the Certificate of Compliance No. 5-2002-00110 dated July 9, 2002, confirming to the Royalty Agreement's compliance with the provisions of Sections 87 and 88 of Chapter IX, Part II of the Intellectual Property Code (Republic Act No. 8293) on Voluntary Licensing *(Exhibit "B")*.

As per petitioner's Monthly Remittance Returns of Final Income Taxes Withheld (BIR Form No. 1601-F) for the period covering January 2002 to June 2002, the following were the final taxes on royalties remitted, computed at 15% pursuant to the "most favored nation clause" of Article 13 (2)(b)(iii) of the RP-US Tax Treaty in conjunction with Article 12 (2) of the RP-Russia Tax Treaty (*pars. 13 & 14, Joint Stipulation of Facts & Issues*), to wit:

Period	Royalty	Amt Paid to Government	Date Due	Date Remitted
Jan-02	33,616,551.87	5,042,487.78	2/11/2002	2/11/2002
Feb-02	108,204,762.13	16,230,714.32	3/11/2002	3/11/2002
Mar-02	187,519,709.93	28,127,956.49	4/10/2002	4/10/2002
Apr-02	186,167,814.67	27,925,172.20	5/10/2002	5/10/2002
May-02	182,805,322.27	27,420,798.39	6/10/2002	6/10/2002
Jun-02	180,316,166.86	27,047,425.03	7/10/2002	7/10/2002
TOTAL	878,630,327.73	131,794,554.21		

On November 18, 1999, the Agreement between the Government of the Republic of the Philippines and the Government of the People's Republic of China for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, or the RP-People's Republic of China Tax Treaty, was signed. Although it was entered into force on March 23, 2001, the provisions relating to taxes on income were applied to those incomes which accrued beginning January 1, 2002.

Consequently, petitioner filed with the Bureau of Internal Revenue-International Tax Affairs Division (BIR-ITAD) on August 7, 2002, a request for the confirmation of the following:

> "a. that the royalties accrued and/or paid by The Coca-Cola Export Corporation, Philippine Branch, (hereinafter the "TCCEC") [Petitioner], to TCCC prior to January 1, 2002 are subject to 15% withholding tax, pursuant to the RP-US Tax Treaty in relation to the RP-Russia Tax Treaty;
>
> b. that the royalties accrued and/or paid by TCCEC [Petitioner] to TCCC beginning January 1, 2002 are subject to 10% withholding tax, pursuant to the RP-US Tax Treaty in relation to the RP-China Tax Treaty." (*par. 1, Joint Stipulation of Facts & Issues*)

In reply to petitioner's inquiry, the BIR-ITAD issued on July 24, 2003 its Ruling Number DA-ITAD-103-03 which states in part that:

> "....royalties arising in the Philippines and payable to TCCC for 2001 are subject to tax at the rate of 15 per cent (15%) while royalty payments accruing beginning January 1, 2002 shall be subject to 10 per cent (10%) pursuant to Article 13(2)(b)(iii) of the RP-US tax treaty, in relation to Article 12 (2)(b) of the RP-Russia and RP-China tax treaties, respectively." (*par. 17, Joint Stipulation of Facts & Issues*)

On the basis of the above BIR-ITAD Ruling, petitioner, on January 12, 2004, filed a formal claim for refund or tax credit of the final taxes on royalties it paid to TCCC covering the period from the beginning of January 2002 to June 2002 in the amount of P43,931,521.44. Petitioner, having received no response to its claim from the respondent, elevated its claim for the same amount to this Court through a Petition for Review on February 6, 2004.

On April 13, 2004, respondent filed his Answer, raising the following as his Special and Affirmative Defenses:

> 4. Petitioner's alleged claim for refund is subject to administrative routinary investigation/examination by the Bureau of Internal Revenue;

5. The amount of P43,931,521.44 being claimed by petitioner as alleged taxes erroneously withheld on royalty payments is not properly documented;

6. In an action for refund/credit, the burden of proof is on the taxpayer to establish its right to refund, and failure to sustain the burden is fatal to the claim for refund/credit;

7. Petitioner must show that it has complied with the provisions of Section 204 (C) and 229 of the 1997 Tax Code on the prescriptive period for claiming tax refund/credit; and

8. Claims for refund are construed strictly against the claimant for the same partake the nature of exemption from taxation (Commissioner of Internal Revenue vs. Ledesma, 31 SCRA 95) and as such, they are looked upon with disfavor (Western Minolco Corp. vs. Commissioner of Internal Revenue, 124 SCRA 1211).

However, on October 4, 2004, petitioner filed an Amended Petition for Review to Conform to Evidence claiming a reduced amount of P37,054,567.02 as the correct amount representing the final taxes withheld on royalties it had paid to TCCC for the period covering January 2002 to June 2002. Respondent did not file an Amended Answer.

After due hearing, this case was submitted for decision on August 12, 2005, taking into consideration petitioner's Memorandum filed on June 3, 2005, sans any Memorandum from the respondent.

The issues to resolved in this case are:

1. Whether or not the petitioner erroneously remitted to the Government the amount of P37,054,567.02 representing final taxes withheld on the royalties it paid to TCCC for the period beginning January 2002 until June 2002; and

2. Whether or not petitioner's claim for refund is properly substantiated.

The crux of the controversy is the proper interpretation of the provisions of the RP-US, RP-Russia, and RP-China Tax Treaties, more particularly, the provisions on the rate of final taxes on royalties, which is to be imposed by the Philippines upon royalties received by a non-resident foreign corporation. For clarity and a better understanding of the provisions of the subject tax treaties, the pertinent articles and provisions are hereunder quoted:

"RP-US TAX TREATY

Article 13

Royalties

1.) Royalties derived by a resident of one of the Contracting States from sources within the other Contracting State may be taxed by both Contracting States.

2.) However, the tax imposed by that Contracting State shall not exceed

a.) In the case of the United States, 15 per cent of the gross amount of the royalties, and

b.) In the case of the Philippines, the least of:

(i) 25 per cent of the gross amount of the royalties;

(ii) 15 per cent of the gross amount of the royalties, where the royalties are paid by a corporation registered with the Philippine Board of Investments and engaged in preferred areas of activities; and

(iii) the lowest rate of Philippine tax that may be imposed on royalties of the same kind paid under similar circumstances to a resident of a third State.

3.) The term "royalties" as used in this Article means payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work, including cinematographic film or films or tapes used for radio or television, broadcasting, any patent, trade mark, design or model, plan, secret formula or process or other like right or property, or for the information concerning industrial, commercial or scientific experience. The term "royalties" also includes gains derived from the sale, exchange or other disposition thereof."

"RP-RUSSIA TAX TREATY

Article 12
Royalties

1. Royalties arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

2. However, the royalties may also be taxed in the Contracting State in which they arise and according to the laws of the State, but the tax so charged shall not exceed 15 per cent of the gross amount of royalties.

3. The term "royalties" shall mean payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work including cinematograph films and films and tapes for television or radio broadcasting, any patent, trademark, design or model, plan, secret formula or process, or for the use of, or the right to use, industrial, commercial or scientific equipment, or for information concerning industrial, commercial or scientific experience."

"**RP-CHINA TAX TREATY**

Article 12
Royalties

1. Royalties arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

2. However, such royalties may also be taxed in the Contracting State in which they arise and according to the laws of the State, but if the recipient is the beneficial owner of the royalties, the tax so charged shall not exceed:

   a. 15 per cent of the gross amount of royalties arising from the use of, the right to use, any copyright of literary, artistic or scientific work including cinematograph films or tapes for television or broadcasting or

   b. 10 per cent of the gross amount of royalties arising from the use of, or the right to use, any patent, trade mark, design or model, plan, secret formula or process, or from the use of, or the right to use, industrial, commercial, or scientific equipment, or for information concerning industrial, commercial or scientific experience.

   For as long as the transfer of technology, under Philippine Law, is subject to approval, the limitation of the tax rate mentioned under (b) shall, in the case of royalties arising in the Republic of the Philippines, only apply if the contract giving rise to such royalties has been approved by the Philippines competent authorities.

3. The term "royalties" shall mean payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work including cinematograph films, or films or tapes for radio or television broadcasting, any patent, trademark, design or model, plan, secret formula or process, or for the use of, or the right to use, industrial, commercial or scientific equipment, or for information concerning industrial, commercial or scientific experience."

Petitioner submits that pursuant to Article 13 of the RP-US Tax Treaty, in relation to Article 12 of the RP-Russia Tax Treaty, it had in fact withheld and remitted to the Government of the Philippines, the concessional tax rate of 15 per cent on royalties paid to TCCC. However, petitioner claims that on the bases of the entry into force of the provisions of the RP-China Tax Treaty regarding taxes on income on January 1, 2002, and "most favored nation clause" found in Article 13 (2)(b)(iii) of the RP-US Tax Treaty, it is now entitled to the lowest tax rate of Philippine tax that may be imposed on royalties of the same kind and paid under similar circumstances to a resident of a third State, which is 10 per cent, pursuant to Article 12 (2)(b) of the RP-China Tax Treaty. To further bolster its claim, petitioner offered in evidence BIR-ITAD Ruling No. DA-ITAD-103-03 which confirmed its opinion that pursuant to the provisions on taxes on income under the RP-China Tax Treaty, petitioner's royalty payments accruing and/or paid beginning January 1, 2002, shall be taxed at the final tax rate of 10 per cent.

This Court agrees.

It must be emphasized that the RP-US, RP-Russia and RP-China Tax Treaties are just a few of the bilateral agreements which the Philippines has entered into for the purpose of avoiding, if not eliminating, double taxation and its effects on the national fiscal legislations of the contracting parties. Double taxation usually takes place when a person is a resident of a contracting state and derives income from, or owns capital in, the other contracting state and both states impose tax on that income or capital (*Commissioner of Internal Revenue vs. S.C. Johnson and Son, Inc., G.R. No. 127105, June 25, 1999*). For this purpose, treaties or agreements on the subject matter entered into then provides for several methods of avoiding from or eliminating double taxations' destructive effects on the free flow of goods and services, as well, as in the movement of capital, technology and persons.

In this instant case, both the Philippines as the state of source, and the United States as the state of residence, are permitted to tax the royalties paid by the petitioner for the right to use TCCC's trademarks, secret processes and formulae, and other confidential know-how relating to or in connection with the manufacture of concentrate beverage bases and syrups. This, undoubtedly, is a case of double taxation. Under the RP-US Tax Treaty, the allowance of a tax credit to citizens or residents of the United States (in a appropriate amount based upon the taxes paid or accrued to the Philippines) against the United States tax, but such tax shall not exceed the limitations provided by United States law for the taxable year, is allowed to give relief from double taxation. On the other hand, under Article 13 thereof, the Philippines is given the choice from three rates, namely: 25% of the gross amount of royalties; 15% when the royalties are paid by a corporation registered with the

Philippine Board of Investment and engaged in preferred areas of activities, or; **the lowest rate of Philippine tax that may be imposed on royalties of the same kind paid under similar circumstances to a resident of the third State.**

In the leading case of **Commissioner of Internal Revenue vs. S.C. Johnson and Son, Inc.,** ***supra***, the Supreme Court interpreted the "most favored nation clause", particularly the phrase "paid under similar circumstances", as referring to the manner of payment of tax, and not to the subject matter of the tax, which is "royalties". In negotiating tax treaties, the underlying rationale for reducing the tax rate is that the Philippines will give up a part of the tax in the expectation that the tax given up for this particular investment is not taxed by the other contracting State. Consequently, the phrase "royalties paid under similar circumstances" in the most favored nation clause of the RP-US Tax Treaty necessarily contemplates "circumstances that are tax-related". The reason for construing this is anchored upon a logical reading of the text in the light of the fundamental purpose of such treaty which is to grant an incentive to the foreign investor by lowering the tax and at the same time crediting against the domestic tax abroad a figure higher than what was collected in the Philippines.

This being so, the provisions of the RP-US, RP-Russia and RP-China Tax Treaties pertaining to royalties should be read together with the provisions on the Avoidance or Relief from Double Taxation. Pertinent provisions of the three treaties are quoted for easy reference, to wit:

"**RP-US TAX TREATY**

Article 23
Relief from double taxation

Double taxation of income shall be avoided in the following manner:

1. In accordance with the provisions and subject to the limitations of the law of the United States (as it may be amended from time to time without changing the general principle thereof), the United States shall allow to a citizen or resident of the United States as a credit against the United States tax the appropriate amount of taxes paid or accrued to the Philippines and, in the case of a United States corporation owning at least 10 per cent of the voting stock of a Philippine corporation from which it receives dividends in any

taxable year, shall allow credit for the appropriate amount of taxes paid or accrued to the Philippines by the Philippine corporation paying such dividends with respect to the profits out of which such dividends are paid. Such appropriate amount shall be based upon the amount of tax paid or accrued to the Philippines, but the credit shall not exceed the limitations (for the purpose limiting the credit to the United States tax on income from sources within the Philippines or on income from sources outside the United States) provided by United States law for the taxable year. For the purpose of applying the United States credit in relation to taxes paid or accrued to the Philippines, the rules set forth in Article 4 *(Source of Income)* shall be applied to determine the source of income. For purposes of applying the United States credit in relation to taxes paid or accrued to the Philippines, the taxes referred to in paragraphs (a)(b) and (2) of Article 1 *(Taxes Covered)* shall be considered to be income taxes.

2. **In accordance with the provisions and subject to the limitations of the law of the Philippines (as it may be amended from time to time without changing the general principle hereof), the Philippines shall allow to a citizen or resident of the Philippines as a credit against the Philippine tax the appropriate amount of taxes paid or accrued to the United States** and, in the case of a Philippine corporation owning at least 5 per cent of the voting stock of a United States corporation from which it receives dividends in any taxable year, shall allow credit for the appropriate amount of taxes paid or accrued to the United States by the United States corporation paying such dividends with respect to the profits out of which such dividends are paid. Such appropriate amount shall be based upon the amount of tax paid or accrued to the United States, but the credit shall not exceed the limitations (for the purpose limiting the credit to the Philippines tax on income from sources within the United States and on income from sources outside the Philippines) provided by Philippines law for the taxable year. For the purpose of applying the Philippines credit in relation to taxes paid or accrued to the United States, the rules set forth in Article 4 *(Source of Income)* shall be applied to determine the source of income. For purposes of applying the Philippines credit in relation to taxes paid or accrued to the United States, the taxes referred to in paragraphs (1)(a) and (2) of Article 1 *(Taxes Covered)* shall be considered to be income taxes."

"<u>RP-RUSSIA TAX TREATY</u>

Article 23
Relief from Double Taxation

In the case of the Philippines, double taxation shall be avoided in the following manner:

Subject to the provisions of the laws of the Philippines relating to the allowance as credit against Philippine tax of tax payable in any country other than the Philippines, income taxes paid or have accrued under the laws of the Russian Federation and in accordance with this Convention, whether directly or by deduction, in respect of income from sources within the Russian Federation shall be allowed as a credit against Philippines tax payable in respect of that income.

In the case of a Philippine corporation owning more than 50 per cent of the voting stock of a Russian company from which it receives dividends in any taxable year, the Philippines shall also allow credit for the appropriate amount of taxes paid or accrued in the Russian Federation to a Russian company paying such dividends with respect to the profits out of which such dividends are paid. The deduction shall not, however, exceed that part of the Philippine income tax, as computed before the deduction is given, which is appropriate to the income which may be taxed in the Russian Federation;

In the case of the Russian Federation, double taxation shall be avoided in the following manner:

Where a resident of the Russian Federation derives income from the Philippines, the amount of tax of that income payable in the Philippines in accordance with the provisions of this Convention, may be credited against the tax levied in the Russian Federation imposed on that resident. The amount of credit, however, shall not exceed the amount of the Russian tax on that income computed in accordance with taxation laws and regulations of the Russian Federation."

"RP-CHINA TAX TREATY

Article 23
Methods for the Elimination of Double Taxation

1. In the Philippines, double taxation shall be eliminated as follows:

Subject to the laws of the Philippines and the limitations thereof regarding the allowance of a credit against Philippine tax of tax payable in any country other than the Philippines. Chinese tax payable in respect of income derived from China shall be allowed as credit against the Philippine tax payable in respect of that income.

2. In China, double taxation shall be eliminated as follows:

Where a resident of China derives income from the Philippines the amount of tax on that income payable in the Philippines in accordance with the provisions of this Agreement, may be credited against the Chinese tax imposed on that resident. The amount of the credit, however, shall not exceed the amount of the Chinese tax on that income computed in accordance with the taxation laws and regulations of China."

Based on the above provisions, the concessional rates of 15% and 10% as provided under the RP-Russia and RP-China Tax Treaties, respectively, should apply only if the taxes imposed upon royalties in the RP-US Tax Treaty, RP-Russia Tax Treaty and RP-China Tax Treaty are paid under similar circumstances. Under Article 23 (1) & (2) Relief from Double Taxation of the RP-US Tax Treaty, it is provided that the allowable foreign tax credit under the treaties is the appropriate amount of taxes actually paid or accrued to the Philippines. Although various tax treaties already in force would show dissimilar provisions on the relief from or avoidance of double taxation as this is a matter of negotiations between the contracting states, a cursory reading of the RP-Russia and RP-China Tax Treaties reveals similar provisions on the relief from or avoidance of double taxation as those stipulated in the RP-US Tax Treaty. There is no provision on a "matching credit" similar to that found in the RP-West Germany Tax Treaty (*Commissioner of Internal Revenue vs. SC Johnson and Son, Inc., supra*). In other words, the three treaties deal with the method of payment by allowing a credit of the foreign tax as against the taxes actually paid in the Philippines, which is considered as paid under similar circumstances. It must be stressed that the purpose of the most favored nation clause is to grant to the contracting state treatment not less favorable that that which has been or may be granted to the "most favored" among other countries. This is intended to establish the principle of equality of international treatment by providing that the citizens or subjects of the contracting nations may enjoy the privileges accorded by either party to those of the most favored nation (*Commissioner of Internal Revenue vs. S.C. Johnson and Son, Inc., supra*).

This likewise finds support in BIR Ruling DA-ITAD No. 103-03 dated July 24, 2003, which provides in part:

> *"In the case of Commissioner of Internal Revenue vs. S.C. Johnson and Son, Inc. and Court of Appeals, G.R.N. 127105, promulgated on June 25, 1999, the Supreme Court interpreted the "most favored nation" clause, particularly the phrase "paid under similar circumstances", as referring to the manner of payment of taxes and not to the subject matter of the tax which is royalties. A perusal of the RP-US, RP-Russia and RP-China tax treaty provisions on the avoidance of double taxation shows a similarity on the manner of payment of taxes, that is, the allowable foreign tax credit on the three treaties is the amount actually paid in the Philippines.*
>
> *Such being the case, and since TCCEC is not registered and engaged in preferred areas of activities in the Philippines, royalties arising in the Philippines and payable to TCCC for 2001 are subject to tax at the rate of 15 per cent (15%) while royalty payments accruing beginning January 1, 2002 shall be subject to 10 per cent (10%) pursuant to Article 13 (2)(b)(iii) of the RP-US tax treaty, in relation to Article 12 (2)(b) of the RP-Russia and RP-China tax treaties, respectively. (BIR Ruling No. DA-ITAD-101-103 dated July 24, 2003; RMC 46-02 dated September 2, 2002)"*

Moreover, Revenue Memorandum Circular No. 46-02, or the Memorandum Circular clarifying the implication of Article 12 (2)(b) on royalties of the RP-China Tax Treaty, which took effect on January 1, 2002 *(Article 28 (2), RP-China Tax Treaty)*, in relation to Article 13 (2)(b)(iii) or the "most favored nation" clause of the RP-US Tax Treaty, confirmed petitioner's stand that the tax on royalties to resident of the United States and China can be considered as paid under similar circumstances.

Clearly then, the provisions of the RP-China Tax Treaty, more particularly, the reduced tax rate on royalties at 10% should apply to petitioner.

As regards the second issue, it is not disputed by respondent that petitioner remitted its payment for the final taxes on the royalties due to TCCC for the period covering January 2002 to June 2002 on the following dates:

Period	Date of Remittance/Payment
Jan-02	2/11/2002
Feb-02	3/11/2002
Mar-02	4/10/2002
Apr-02	5/10/2002
May-02	6/10/2002
Jun-02	7/10/2002

Pursuant to Section 229 of the 1997 National Internal Revenue Code, no suit or proceeding for refund shall be filed after the expiration of two (2) years from the date of payment of the tax or penalty regardless of any supervening cause that may arise after payment. Accordingly, petitioner has a period of two (2) years from the date of payment or remittance within which to file its claim for refund or issuance of a tax credit certificate. Thus, for the final taxes on royalties paid on February 11, 2002, March 11, 2002, April 10, 2002, May 10, 2002, June 10, 2002 and July 10, 2002 to cover the months of January to June 2002, petitioner had until February 11, 2004, at the earliest, to file both its administrative and judicial claims for refund. Petitioner filed its administrative claim for refund on January 12, 2004 (*par. 18, Joint Stipulation of Facts & Issues*) and this instant petition on February 6, 2004, which are undoubtedly well within the two-year prescriptive period.

With regard to the amount claimed by petitioner, an Amended Petition for Review to Conform to Evidence was filed by petitioner, thereby showing a reduced claim of P37,054,567.02. Petitioner submits that the error arose from its discovery that the total royalty actually owed to TCCC for the months of January to June 2002 amounted to

P947,399,821.96 and not P878,630,327.73 as reflected in its Monthly Remittance Returns of Final Taxes Withheld. However, notwithstanding the errors which arose particularly for the months of April and June 2002, there was still no under-payment of the final taxes on royalties for the said period.

After a careful analysis of the arguments and evidence presented, both documentary and testimonial, it is clear that petitioner has fully satisfactorily substantiated its claim for refund in the amount of P37,054,567.02.

Revenue Memorandum Circular No. 46-02, requires the twin compliance of the following before the reduced tax rate of 10% may be availed of by the taxpayer invoking the same. To quote:

> "1. *It is necessary that there be an agreement or a contract whereby the royalties paid to the US must originate from the use of, or the right to use any patent, trade mark, design or model, plan, secret formula or process, or from the use, or the right to use, industrial, commercial or scientific experience; and*
>
> 2. *For as long as the contract or agreement is subject to approval under Philippine law, the same must be duly approved by the Philippine competent authority."*

In compliance with the requirements under RMC 46-02, petitioner offered in evidence the Royalty Agreement entered into by and between the petitioner and TCCC, and duly authenticated by the Philippine Consulate in Atlanta, Georgia on July 2, 2002 *(Exhibit "A")* and the Certificate of Compliance No. 5-2002-00110 issued by the Philippine Intellectual Property Office dated July 9, 2002 *(Exhibit "B")*. Under this agreement, petitioner was able to satisfactorily show that the parties have agreed to the conditions, as set forth therein, for the petitioner's payment of royalty or license fees to TCCC for the "use by petitioner of the trademarks, the secret processes and formulae for the manufacture of the Products, and other confidential know-how, and for the use of other intangibles" *(Exhibit "A")*. Likewise, the Certificate of Compliance duly confirmed the compliance of the Royalty Agreement with the provisions of R.A. No. 8293 (Intellectual Property Code) on Voluntary Licensing.

Anent petitioner's computation of the taxes remitted and allegedly overpaid, it was established that petitioner's total withholding tax payment on royalties per its Monthly Remittance Returns for the months of January 2002 to June 2002 amounted to P131,794,549.21 (P878,630,327.73 x 15%) (*par. 14, Joint Stipulation of Facts & Issues; p. 54, TSN dated August 9, 2004*), based on the tax rate of 15%, pursuant to the RP-US and RP-Russia Tax Treaties. However, upon proper verification, and as testified to by petitioner's Financial Reporting Manager and witness, Karen Obciana-Magbanua, which data was likewise certified to as correct by the Vice-President and General Tax Counsel of TCCC, Steve M. Whaley (*Exhibit "GG"*), the royalty expense for the months of April and June 2002 should have reflected the amounts of P215,124,231.00 and P220,129,247.73, respectively (*Exhibit "EE"*), giving rise to a total royalty expense of P947,399,821.95 for the periods covering January to June 2002. In effect, the final taxes on royalties for the same months should be P21,512,423.10 and P22,012,924.77, respectively (*Exhibit "EE"*).

Nevertheless, these errors did not result in an under-payment of final taxes on royalties considering that the tax rate of 15% used by petitioner in its computation should have been at the reduced rate of 10%. Thus, based on the corrected amount of royalty expense, that is, P947,399,821.95, petitioner only owed the Government of the Philippines the final tax on royalties of P94,739,982.19 (P947,399,821.95 x 10%) based on the concessional rate of 10% pursuant to the RP-China Tax Treaty. Consequently, petitioner still had an over-payment of P37,054,567.02 (P131,794,549.21 - P94,739,982.19).

IN VIEW OF THE FOREGOING, the subject Petition for Review is hereby **GRANTED.** Accordingly, respondent is **ORDERED TO REFUND** or in the alternative, **ISSUE A TAX CREDIT CERTIFICATE** in favor of petitioner in the amount of **P37,054,567.02** representing over-payment of final taxes on royalties withheld for the period covering January 2002 to June 2002.

SO ORDERED.

ERNESTO D. ACOSTA
Presiding Justice

WE CONCUR:

LOVELL R. BAUTISTA
Associate Justice

CAESAR A. CASANOVA
Associate Justice

CERTIFICATION

Pursuant to Article VIII, Section 13 of the Constitution, it is hereby certified that the conclusions in the above Decision were reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

ERNESTO D. ACOSTA
Chairperson, First Division
Presiding Justice