RARY

REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

DOWELL SCHLUMBERGER
(EASTERN), INC. -
PHILIPPINE BRANCH,
Petitioner,

- versus - C.T.A. CASE NO. 3786

THE COMMISSIONER OF
INTERNAL REVENUE,
Respondent.

x - - - - - - - - - - - - - - - - x

DOWELL SCHLUMBERGER,
INC.,
Petitioner,

- versus - C.T.A. CASE NO. 4042

THE COMMISSIONER OF
INTERNAL REVENUE,
Respondent.

Promulgated:
JAN 26 1995

x - x

D E C I S I O N

Dowell Schlumberger (Eastern), Inc., petitioner in these two cases filed two petitions, one claiming for the refund and/or tax credit of allegedly overpaid income and erroneously withheld taxes for the calendar year 1982 in the amount of P1,407,852.00 (C.T.A. Case No. 3786); and the other claiming for the refund of alleged erroneously paid contractor's tax of P531,931.76, for the calendar year 1984 or in the alternative a lesser amount of P389,325.63, should the Court find it liable for contractor's tax under Section 205 of the Tax Code (C.T.A. Case No. 4042).

As gleaned from the records and the pleadings of the parties, it appears that petitioner is a resident foreign corporation doing business in the Philippines. It provides directional drilling tools and services as a sub-contractor of service contractors engaged in petroleum operations in the Philippines. The facts are narrated as follows:

FACTS:

C.T.A. CASE NO. 3786

On January 1, 1982, petitioner entered into a Contract For Cementation Services with PNOC-EDC whereby the former agreed to provide the latter with cementing equipment and services (Exh. A). On same date, both parties entered in another Contract For Directional Drilling Services where petitioner would provide

PNOC-EDC with directional drilling tools and services (Exh. B). In both instances, said contracts were entered into by PNOC-EDC in connection with the petroleum service operations of PNOC-EDC as the prime contractor of the government under Presidential Decree No. 1354 [Imposing Final Income Tax on Subcontractors And Alien Employees Of Service Contractors and Subcontractors Engaged In Petroleum Operations In The Philippines Under Presidential Decree No. 87].

For the year 1982, petitioner is likewise engaged in non-Presidential Decree No. 1354 services to various clients among which was PNOC-EDC. PNOC-EDC withheld from petitioner the 8% final income tax on the gross receipts received by petitioner from both the P.D. 1354 services covering the petroleum operations as well as the non-P.D. 1354 services rendered by petitioner. For the non-P.D. 1354 services, PNOC-EDC withheld the 8% final income tax on its payments to petitioner in the total amount of P1,407,852.00. It would appear from the records that petitioner incurred a net loss from its operations, covering the non-P.D. 1354 services, in the amount of P3,118,845.00 (Exh. C) and therefore, no income tax liability was due therefrom. In effect, petitioner had allegedly overpaid its income tax in 1982 by P1,407,852.00, representing the 8% final tax withheld by PNOC-EDC on services rendered by petitioner with respect to PNOC-EDC's non-P.D. 1354 operations.

On May 9, 1984, petitioner through its auditors filed a claim for refund or tax credit (Exh. R) with the respondent in the amount of P1,407,852.00, itemized as follows: (Exh. C-3)

DOWEL SCHLUMBERGER (EASTERN), INC. - PHILIPPINE BRANCH
SCHEDULE OF TAX WITHHELD BY CLIENTS
DECEMBER 31, 1982
(NON-P.D. 1354)

Client	Date Paid To BIR	RTR No.	C.R. No.	Gross Amount	Tax Withheld
PNOC-EDC	5/10/82	9248722	9169448	P4,220,738.63	P 337,659.09 *
	6/10/82	9499257	9168699	3,764,207.83	301,136.63 *
	9/10/82	9876704	10353359	7,098,200.51	537,918.00
	10/10/82	9999314	10353663	2,573,558.38	204,037.15
	11/10/82	10140783	10628983	2,015,066.13	161,205.29
	12/10/82	10182549	10629297	1,962,114.33	156,037.23
				P21,633,885.81	P1,697,993.39

Less: Taxes claimed under P.D. No. 1354 returns 290,141.39

TOTAL CLAIMABLE TAX CREDIT IN NON-P.D. 1354 RETURNS P1,407,852.00

* P337,659.09
301,136.63
P638,795.72
290,141.39 - Claimed under P.D. 1354 returns

P348,654.33 - Net applicable to non-P.D. 1354

Respondent has not acted on such claim. Hence, the present petition for review docketed as C.T.A. Case No. 3786.

C.T.A. CASE NO. 4042

On October 16, 1981, the Government of the Republic of the Philippines, represented by the Ministry of Energy (MOE) through the Bureau of Energy Development, entered into a Service Contract (Geothermal Resources) with PNOC-Energy Development Corporation (PNOC-EDC) as the contractor who shall furnish the necessary services, technology and financing for the geothermal operations of the Government (Exh. A).

On January 1, 1983, PNOC-EDC entered into a contract with Dowell Schlumberger (Eastern), Inc. - Philippine Branch, petitioner in these two cases, to do the drilling and cementing services in connection with the exploration, development and production of geothermal resource in certain areas designated by PNOC-EDC (Exh. B). Petitioner agreed to provide the labor, materials, supplies and all things necessary to perform the work, including the furnishing for its own use the tools, instruments, accessories and equipment. Likewise, it undertakes to provide the workers and personnel under its employ.

For the calendar year 1984, petitioner paid directly with the BIR 3% contractor's tax in the total amount of P342,208.08 as evidenced by its Quarterly Percentage Tax Returns for the first, second and third quarters of 1984 (Exhs. C-1, D-1 and E-1) and their corresponding BIR Payments Order and CB Confirmation Receipts (Exhs. C-2, C-3, D-2, D-3, E-2 and E-3). Aside from the contractor's tax it paid directly to the BIR, PNOC-EDC withheld from petitioner 3% contractor's tax in the sum of P189,723.68 (Exhs. C-7 to C-19; F-1 and F-5 to F-13). Petitioner paid the contractor's tax in the total amount of P531,931.76, breakdown appearing in Exh. G-8.

On March 5, 1986, petitioner through its auditors filed a claim for refund with the BIR in the amount of P531,931.76, representing erroneously paid 3% contractor's tax for the year 1984. It is petitioner's opinion that as a sub-contractor it is not liable for contractor's tax under Section 205 of the Tax Code.

However, in the event the BIR rule otherwise, petitioner is still entitled to the refund of P389,325.63, computed as follows:

Gross Receipts declared in 1984	P11,984,854.33
Add: Additional Receipts previously declared	21,779.25
Total	P12,006,633.58
Less: Receipts paid out of proceeds of foreign loans contracted by PNOC-EDC pursuant to P.D. # 334 as amended by P.D. # 572 which are exempt from contractor's tax	7,085,052.83
Receipts which are merely recharges to or reimbursements from PNOC-EDC	168,042.84
Gross Receipts which should have been subjected to contractor's tax	P 4,753,537.91
Contractor's Tax Due	P 142,606.13
Less: Contractor's Tax Paid	531,931.76
Claim for Refund	P 389,325.63

Respondent did not act on the refund claim filed by petitioner. Hence, petitioner filed on March 24, 1986 a petition for review docketed as C.T.A. Case No. 4042.

In her affirmative and special defenses, respondent in both cases contended that petitioner has the burden of showing that the taxes paid were erroneously or illegally collected. Taxes are presumed to have been collected in accordance with law.

After the presentation of petitioner's exhibits in support of its claim for refund and/or tax credit of overpaid withholding tax for the calendar year 1982 in C.T.A. Case No. 3786 and the claim for refund of erroneously paid 3% contractor's tax for the calendar year 1984 in C.T.A. Case No. 4042, respondent waived the presentation of her evidence. Instead, respondent submitted these cases for decision based on the pleadings and the records offered by petitioner in both cases.

ISSUES:

C.T.A. Case No. 3786:

Whether or not petitioner is entitled to the refund of P1,407,852.00 allegedly representing overpayment of income tax for its non-Presidential Decree No. 1354 services for the year 1982.

C.T.A. Case No. 4042:

Whether or not petitioner is entitled to the refund of P531,931.76 allegedly representing erroneously paid contractor's tax or in the alternative the refund of P389,325.63 as overpaid contractor's tax for the year 1984.

C.T.A. Case No. 3786:

The laws applicable in this case are Sections 1 and 3(a) of Presidential Decree No. 1354 (April 21, 1978) and Section 1(e) of Revenue Regulations No. 13-78 (September 7, 1978).

Sections 1 and 3(a) of Presidential Decree No. 1354, provides:

> "SECTION 1. ***Tax on subcontractors.*** - Every subcontractor, whether domestic or foreign, entering into a contract with a service contractor engaged in petroleum operations in the Philippines shall be liable to a final income tax equivalent to eight percent (8%) of its gross income derived from such contract, such tax to be in lieu of any and all taxes, whether national or local: *Provided, however,* that any income received from all other sources within and without the Philippines in the case of domestic subcontractors and within the Philippines in the case of foreign subcontractors shall be subject to the regular income tax under the National Internal Revenue Code. The term "gross income" means all income earned or received as a result of the contract entered into by the subcontractor with a service contract engaged in petroleum operations in the Philippines under Presidential Decree No. 87. (Underscoring supplied.)

x x x x x x x x x.

> "SEC. 3. ***Manner of collecting the tax*** - (a) Every service contractor shall deduct, withhold, and pay the tax imposed in Section 1 of this Decree from the amounts paid by the service contractor to the subcontractor under the contract entered into by and between them in the same manner and subject to the same conditions as provided in Section 54 of the National Internal Revenue Code."

Section 1(e) of Revenue Regulations No. 13-78 (September 7, 1978), [Supplemented by Rev. Regs. No. 6-79 dated June 4, 1979 and amended by Rev. Regs. Nos. 13-81 (May 29, 1981), 3-82 (April 13, 1982), 4-82 (March 25, 1982), 5-82 (August 4, 1982)] provides:

> "**Section 1. Income payments subject to withholding tax and rates prescribed therein.** - Except as herein otherwise provided, there shall be withheld a creditable income tax at the rates herein specified for each class of payee from the following items of income payments to persons residing in the Philippines:
>
> x x x x x x x x x.
>
> **(e) Amounts paid to certain contractors.** - On gross payments to the following contractors, whether individual or corporation - three *per centum* (3%):
>
> (1) General engineering, general building and specialty contractors -
>
> x x x x x x x x x."

Section 1 of Presidential Decree No. 1354 makes it plain that the 8% final income tax refers only to the gross receipts/income derived by a sub-contractor from service contractor engaged in petroleum operations in the Philippines. All other income received from sources other than petroleum operations are subject to the regular income tax rates under the National Internal Revenue Code. In relation to this, Section 1(e) of Revenue Regulations No. 13-78, provides for the withholding tax of 3% on gross payments received by general engineering, general building and specialty contractors. Thus, for non-P.D. 1354 services rendered by petitioner to PNOC-EDC, the latter should have withheld only 3% instead of 8% final income tax under P.D. 1354.

Inasmuch as petitioner suffered a net loss from its non-P.D. 1354 services, then the tax withheld by PNOC-EDC on petitioner's non-P.D. 1354 operations in the amount of P1,407,852.00 represented an overpayment of income tax as well as an erroneously withheld tax. After having proved entitlement to the refund and/or credit of P1,407,852.00 by presenting voluminous invoices covering the taxes withheld, We find no reason why the same should not be granted in favor of petitioner.

<u>C.T.A. Case No. 4042:</u>

The word "contractor" when standing alone or not restrained by the context or particular words, may mean a sub-contractor, or any person, remotely engaged under contract and doing the work, as well as the original contractor. Such a person is a contractor as well as the original contractor. **(Epifanio G. Gonzales, National Internal Revenue Code, 1984 Revised Edition, p. 527.)** It was formerly held that a contractor and sub-contractor are independent taxpayers and are separately taxable. The payment of the contractor's tax by the prime contractor does not exempt the sub-contractor, who actually did the construction job, from his own liability to pay the percentage tax. **(P. J. Kiener Co., Ltd. v. Commissioner of Internal Revenue, G.R. No. L-16417, January 31, 1963, 7 SCRA 75.)** However, this is now subject to the last paragraph of Section 205 of the Tax Code, which reads:

> "The term 'gross receipts' means all amounts received by the prime or principal contractor as the total contract price, undiminished by amount paid to the subcontractor under a subcontract arrangement.. Any portion of the total contract price which is paid to the subcontractor, shall be excluded from the taxable gross receipts of the subcontractors. (As amended by P.D. No. 1457.)"

We have interpreted the above-mentioned definition in the case of **Dravo Philippines, Inc. v. Commissioner of Internal Revenue, C.T.A. Case No. 3487, September 15, 1989,** as follows:

> "x x x. The statute speaks of the portion of the contract price paid to the subcontractor under a subcontract agreement as excluded from the taxable gross receipts of such subcontractor. Accordingly, for the exclusion to apply, it is enough that the gross receipts are those of a subcontractor and they form part of the portion of the total contract price of the prime or principal contractor paid to such subcontractor. That the subcontractor may be an independent contractor, to our mind, is therefore of no moment. It seems clear that the philosophy behind the exclusion is to minimize the effects of double taxation of the same gross receipts."

In the case at bar, petitioner paid directly the BIR contractor's tax of P342,208.08 and P189,723.68 was withheld by PNOC-EDC (principal contractor) or a total of P531,931.76 was paid on its gross receipts arising from the Service Contract between PNOC-EDC and petitioner as sub-contractor. Section 205 is clear on the definition of "gross receipts". Gross receipts paid to petitioner as sub-contractor are excluded from its taxable gross receipts as a sub-contractor.

In its claim for refund filed with the BIR, it stated that all the receipts earned by petitioner in 1984 were proceeds from their contract with PNOC-EDC. Since the gross receipts paid to petitioner as sub-contractor are excluded under Section 205 of the Tax Code, then the same should not be subjected to the contractor's tax. Only the other receipts earned by the sub-contractor as prime contractor is subject to the contractor's tax. The portion of the total contract price which is paid to the sub-contractor shall be excluded from the taxable receipts of the sub-contractor. All the proceeds earned from its sub-contract agreement with PNOC-EDC does not form part of the gross receipts of petitioner as sub-contractor subject to the contractor's tax. Petitioner is entitled to the refund claimed in the amount of P531,931.76.

WHEREFORE, in view of the foregoing, the petitions for review are found to be meritorious and the same are hereby **GRANTED.** Respondent is hereby ordered to refund in favor of petitioner the amount of P1,407,852.00, representing overpaid withholding taxes for the calendar [illegible] services under C.T.A. Case No. 3786. In addition, respondent is also ordered to refund in favor of petitioner the amount of P531,931.76, representing erroneously paid 3% contractor's tax for the calendar year 1984, under C.T.A. Case No. 4042.

No costs of suits.

SO ORDERED.

RAMON O. DE VEYRA
Associate Judge

WE CONCUR:

ERNESTO D. ACOSTA
Presiding Judge

MANUEL K. GRUBA
Associate Judge

CERTIFICATION

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

ERNESTO D. ACOSTA
Court of Tax Appeals
Presiding Judge