REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

BOISE CASCADE PHILIPPINES, INC.,
Petitioner,

- versus - C.T.A. CASE NO. 2858

COMMISSIONER OF INTERNAL REVENUE,
Respondent.
x - - - - - - - - - - - - - - x

3/30/87

D E C I S I O N

This case involves an appeal by the petitioner to this Court from two (2) adverse decisions of respondent Commissioner of Internal Revenue dated January 28, 1977 (Exh. E, pp. 237-238, BIR rec., Folder I.) and January 25, 1977. (Exh. Z, pp. 132-133, BIR rec., Folder II.)

The first decision refers to a deficiency income tax assessment covering the fiscal years June 30, 1966 and 1967, and calendar year ended December 31, 1967 and deficiency withholding tax for the same years in the amounts of ₱711,025.52 and ₱870,464.73, respectively; while the second decision involves a deficiency withholding tax-at-source against petitioner in the amount of ₱451,976.86 for the calendar year ended December 31, 1968.

Petitioner is a corporation duly organized and existing under the laws of the Philippines. It was incorporated on August 27, 1965 as a subsidiary of Boise Cascade International (TSN., p. 13, December 12, 1977; Ibid, p. 68, August 11, 1980) a foreign corporation. Its main business consists in the building, manufacturing, producing and selling of all kinds of paper products.

Sometime in 1964, the USAID, which had quite an extensive investment in the corporation known as the Bataan Pulp & Paper Mills Inc. (hereinafter referred to as BATAAN for short), which is also engaged in the same business of manufacturing paper products, sought the financial aid of the petitioner herein, as BATAAN is then already in the verge of bankruptcy. (TSN., pp. 9-10, April 11, 1980; Ibid., pp. 78-80; Ibid., pp. 112-113, August 11, 1980). Equally, the Zamboanga Wood Products, Inc. (hereinafter referred to as ZAMBOANGA for short), also a domestic corporation engaged in the business as manufacturer of building products, such as plywood and others, was equally forced to approach also the

Boise Cascade International in 1965 for financial aid inasmuch as it was also in bad financial situation and in the verge of business collapse. Because of these circumstance, it gave an impetus for the organization of petitioner-corporation, the Boise Cascade Philippines, Inc. (hereinafter known as BOISE CASCADE PHILIPPINES, for brevity) in August 1965. (TSN, p., 112, August 11, 1980.) with the specific functions, purposes and objectives of providing technical know-how of and direct the management of the said two domestic corporations, BATAAN and ZAMBOANGA, and thereby rehabilitate and salvage them from their respective business failures. (TSN, pp. 79-80, Aug. 11, 1980.)

Petitioner, as manager of the two corporations, BATAAN and ZAMBOANGA, decided to obtain funds for said corporations so as to make possible their continued business operations by means of loans secured from its parent company, the Boise Cascade International (hereinafter referred to as BOISE INTERNATIONAL for short) and reloaning the money secured from the latter to the said distressed companies.

(TSN, pp. 8-9, April 11, 1980).

The first loan secured and dated November 1, 1965 (Exh. G, found in petitioner's Envelope) was in the amount of ₱1,920,200.00. This loan was secured under a contract entered into by and between petitioner and its parent company, the BOISE INTERNATIONAL, which contract provides that petitioner shall be obligated to repay the said loan on or before September 1, 1970, with interest at 12% per annum. (TSN., pp. 19-20, December 12, 1977).

The second loan secured as aforesaid dated November 6, 1965 (see Exh. H, found petitioner's envelope) was in the amount of ₱600,000.00 which contract of loan was similarly executed by and between petitioner and its parent company, the BOISE INTERNATIONAL, and this contract of loan provides that petitioner shall pay the loan within thirty days from the date of the demand of payment, with interest of 12% per annum, (TSN., pp. 20-22, December 12, 1977).

Lastly, a loan, in the amount of ₱11,400,000.00 dated January 5, 1967 (Exh. F, pp. 25-26, BIR rec. Folder I) was entered into by and between petitioner and the BOISE INTERNATIONAL, which contract provides that petitioner shall repay the above mentioned loan within one year after demand is made, with interest at 8 3/4% per annum.

At this juncture, it is to be noted that pursuant to the existing Central Bank Rules & Regulations, the aforesaid three (3) loans secured by petitioner were accepted and approved for registration as loans secured from the BOISE INTERNATIONAL by petitioner. (Exh. J, petitioner's envelope).

The evidence show that the aforesaid amount of ₱600,000.00 was later reloaned by petitioner to BATAAN (TSN. p. 86, Aug. 11, 1980); while the amount of ₱11,400,000.00 was later reloaned to ZAMBOANGA (TSN. p. 83, Aug. 11, 1980). However, the amount of ₱1,920,200.00 (Exh. G) was merely held by petitioner as stand-by or reserve fund which it can and may reloan from time to time either to said BATAAN or ZAMBOANGA as the case may be, on a short term basis, whenever said companies will find themselves short of their operational expenses. (TSN, pp.87-88, Aug. 11, 1980) It is further noted that all these amounts loaned by petitioner were reflected in its books of account and financial statements as its liabilities or as loans payable to the BOISE INTERNATIONAL. (TSN., pp. 69-70, Aug. 11, 1980; Ibid., pp. 117-120, Oct. 2, 1980; Ibid., pp. 17-23, April 11, 1980). The interests that accrued or were due on the aforesaid loans were also reflected not only in petitioner's books of account, but also in its audited financial statements covering the years in question. (Ibid., TSN, pp. 120-122, Oct. 2, 1980). As regards the interest incomes earned from the amounts reloaned by petitioner to BATAAN and ZAMBOANGA, these items of interests were likewise reflected as income in its book of account (TSN, pp. 121-122, Oct. 2, 1980), as well as in the audited financial statements for the years in question. (TSN., pp. 31-34, April 11, 1980.)

As we have said earlier, the aforesaid loans evidenced by promissory notes, which were executed by petitioner in favor of BOISE INTERNATIONAL, were registered and approved by the Central Bank of the Philippines in 1970. (Exh. J, Petitioner's big envelope). Thus, on the amount of ₱600,000.00 loan (later reduced to ₱400,000.00) (p. 122, TSN, Oct. 2, 1980) and which was reloaned to BATAAN aforesaid, petitioner started accruing interest due on the said loan from November 5, 1965 to August 1970 on an annual basis. However, it was only on September 5, 1970 that said petitioner was able to remit to the BOISE INTERNATIONAL 65% of the interests income earned. It was also on that date that the 35% withholding tax on such interest remitted was paid under Receipt No. 2323927. (Exhs. AA, EE, EE-1, found in petitioner's big envelope; Exh. T-1, p. 187, Folder II, BIR rec.; TSN, pp. 46-48, May 27, 1980.)

As regards the loan in the amount of ₱1,920,200.00, the petitioner started accruing the interest due thereon from November 1965 on an annual basis up to December 31, 1968 which amounted to ₱691,271.81. Additional interests also accrued in the following years but it was only on October 2, 1970 that petitioner was able to effect the first partial remittances of the interest on November 12, and December 12, 1970. The corresponding interests accruals, and the 35% withholding taxes were paid by petitioner as at the time when the remittances were made to BOISE INTERNATIONAL. (Exhs. BB, FF, on petitioner's big envelope; see also Exhs. T-2, T-3, T-4, T-5 & T-6, pp. 186-187 BIR rec., Folder II; TSN., pp. 49-54, May 27, 1980.)

The same is true in the case of the petitioner's loan in the amount of ₱11,400,000.00. The interest thereon was accrued on annual basis, but the remittances of the interest thereon were made only beginning October 11, 1971, and the corresponding withholding taxes were paid as at the time the remittances were made out to said BOISE INTERNATIONAL. (Exhs. CC, GG, found in petitioner's big envelope; Exhs. T-8, p. 185, BIR rec., Folder II; TSN., pp. 55-58, May 27, 1980.)

Sometime on January 12, 1967, petitioner herein filed its amended income tax return for the year 1966. (Exh. K, p. 80, BIR rec., Folder I). In a letter dated April 3, 1972 (Exh. C, pp. 194-196 BIR rec., Folder I), respondent assessed petitioner for deficiency income and withholding taxes covering fiscal years June 30, 1966 and June 30, 1967 as well as calendar year ended December 31, 1967, which assessment appears to have been released by respondent on April 12, 1972 (Exhs. C-1, p. 194 BIR rec., Folder I.), computed as follows:

ACR-400141-71/66

Net income per return	₱417,421.02
Add: Unallowable deduction	
Interest expense dividends	364,814.10
Net income per investigation	782,235.02
Tax due thereon	226,671.00
Less: Amount already assessed	117,226.00
Balance	₱109,445.00
Add: ½ mo. int. fr. 10-16-66 to 10 16-69	19,700.10
Total amount due and collectible	₱129,145.10

ACR-600097-71/67

Net income per return	₱ 77,732.50
Add: Unallowable deduction-	
Interest expense dividend	1,025,280.18
Net income per investigation	₱1,103,012.68
Tax due thereon	₱ 322,904.00
Add: ½ mo. int. fr. 10-16-67 to 10-16-70	54,936.54
Total amount due and collectible ...	₱ 360,139.54

CAL-ACR-600396/67

Net income per return	₱ 52,848.72
Add. Unallowable deduction-	
Interest expense dividend ...	638,962.00
Net income per investigation	691,543.00
Tax due thereon	199,543.00
Less: amount already assessed	11,627.00
Balance	₱ 187,916.00
Add: ½ mo. int. fr. 4-16-68 to 4-16-71	33,824.88
Total amount due & collectible	₱ 221,740.88

FY-6-30-66

Total amount remitted	₱ 364,814.00
30% withholding tax at source	109,444.00
Add: 25% surcharge	27,361.00
½ mo. int. fr. 10-16-66 to 10-16-69	19,699.92
Total amount due & collectible	₱ 156,504.92

FY-30-67

Total amount remitted	₱	1,025,280.18
30% withholding tax at source		307,584.00
Add: 25% surcharge		76,896.00
½% mo. int. fr. 10-16-67 to 10-16-70		55,365.12
Total amount due & collectible	₱	439,845.12

Calendar Year 1967

Total amount remitted	₱	638,962.00
30% withholding tax at source		191,688.60
Add: 25% surcharge		47,922.15
½% mo. int. fr. 4-16-68 to 4-16-71		34,503.94
Total amount due & collectible	₱-	274,114.69

Respondent, in another letter dated September 15, 1972, assessed petitioner for the year 1968 holding the latter liable for deficiency withholding income tax in the total amount of ₱451,976.86 (Exh. X, p. 108, BIR rec., Folder II), computed as follows:

Interest income of Boise Cascade International Inc., of New York, USA, mother company of Boise Cascade Philippines, Inc. subject to withholding tax and claimed as an expense in the income tax return of the local corporation	₱1,275,923.99
Total withholding tax due for the year 1968	₱ 382,777.00
Add: ½% mo. int. fr. 4/16/69 to 4/16/72	68,899.86
Penalty for failure to file return and to pay tax	300.00
TOTAL DEFICIENCY WITHHOLDING INCOME TAX ...	₱ 451,976.86

The income tax deficiency assessment issued by respondent was based on the disallowed item of interest expenses claimed by petitioner in its income tax returns for the years in question on the ground that the aforesaid interest expenses were considered disguised dividend distributions. The withholding tax deficiency assessment on the other hand was made by respondent on the ground that the duty to withhold and pay the tax arises upon accrual of the income in the books of accounts of petitioner and not at the time of actual payment or remittance thereof.

In a letter dated May 5, 1972, which was received by respondent on May 8, 1972 (Exh. D, pp. 202-213, BIR rec., Folder 1), petitioner disputed the respondent's assessment dated April 3, 1972 on the following grounds:

1. As to the Deficiency Income Tax: Petitioner contends that the interest payments were not disguised dividends but were in reality payments of interest on a bona-fide indebtedness by petitioner to the BOISE INTERNATIONAL.

2. As to the Deficiency Withholding Tax: Petitioner contends that until an actual payment or

remittance of the interest income is actually made to BOISE INTERNATIONAL, it cannot be considered as income of a non-resident foreign corporation and, therefore, when said interest income is not yet remitted, it is not subject to withholding tax especially so where the remittance thereof is restrained by Central Bank restrictions.

And also, in a letter dated October 16, 1972, petitioner equally contested respondent's deficiency withholding tax assessment of September 15, 1972, which was received by respondent on October 17, 1972 (Exh. Y, pp. 119-123 BIR rec., Folder II) for the year 1968, on the ground that no actual remittance of interest was made in 1968 and the remittances to BOISE INTERNATIONAL of the interest incomes in the amount of ₱1,275,903.99 were effected only in the years 1970-1971. And it was only upon the actual remittance of the interest income due to BOISE INTERNATIONAL can petitioner withhold and remit to the government the corresponding 35% withholding tax on such income and the mere accrual of interest expense in petitioner's books of account will not subject such income to withholding tax if no actual remittance is made thereof to the foreign corporation, such as the BOISE INTERNATIONAL in this case.

In a letter dated January 25, 1977 (Exh. Z, pp. 132-133, BIR rec., Folder II), respondent denied petitioner's letter of protest dated October 16, 1972 pertaining to the amount of ₱451,976.56 as deficiency withholding tax-at-source for the year 1968; and also, respondent, in his letter dated January 28, 1977 (Exh. E, pp. 237-238, BIR rec., Folder I), denied petitioner's letter of protest dated May 5, 1972; and that in these two separate letters of denial, respondent reiterated the payment of the said deficiency assessments. Hence, on February 22, 1977, petitioner appealed to this Court.

On April 1, 1977, respondent filed his answer to the aforesaid petition for review, and by way of special and affirmative defenses (pp. 15-16, CTA rec.) asserted the following allegations:

> 6. The alleged promissory notes that petitioner has conveniently devised for Boise Cascade International, Inc., cannot give rise to a debtor-creditor relationship between them because of the absence of a fixed maturity date for repayment (Alamoritas Cattle Corp. vs. Campbell, 9 AFTP 2d 1446; Atlantic Acceptance Corp. vs. Tomlison, 7 AFTR 2d 5965);

7. Petitioner herein is 99.24% owned by Boise Cascade International, a foreign corporation not authorized to engage in trade or business in the Philippines;

8. As the capital stock of petitioner is practically owned by Boise Cascade International, the amounts paid by the former to the latter allegedly in the form of interests were actually distribution of dividends;

9. The assessments in the sums of ₱870,464.73 and ₱451,976.86 representing withholding tax at source are not dependent on remittance of the income payable to the non-resident foreign corporation. The duty to withhold arises upon accrual thereof (BIR Ruling No. 71-003, February 26, 1971;

10. The assessments were issued in accordance with law and regulations.

The issues presented before Us for determination are as follows:

1. Whether or not petitioner's payments of interests to Boise Cascade International under the three promissory notes are disguised dividends;

2. Whether or not respondent's right to assess petitioner for Fiscal Year ended June 30, 1968 has prescribed;

3. Whether or not petitioner has already paid the withholding income taxes that are the subject of the deficiency withholding tax assessments;

4. Whether or not the obligation to withhold and pay income tax on interest payments due a non-resident recipient is upon accrual of such interest income or upon the actual remittance or payment thereof; and

5. Whether or not petitioner is liable to 25% surcharge and interest imposed upon it by the respondent.

As regards <u>the first issue</u>, it is to be noted that the deficiency income tax assessment was the direct result of the disallowance of interest deductions claimed by petitioner in its income tax returns in the amount of ₱364,814.00 for fiscal year beginning June 30, 1966; ₱1,025,280.18 for fiscal year beginning June 30, 1967; and ₱638,962.00 for year ended December 31, 1967. The said disallowances were based on respondent's theory that the interest payments were actually dividend distributions to BOISE INTERNATIONAL for the reason that said Boise Cascade International owns 99.24% of the capital stock of the petitioner herein and that the promissory notes executed by petitioner in favor of Boise Cascade International has no fixed maturity date. It is further contended that the transactions were actually investments made by Boise Cascade International in the guise of loans to petitioner and that it was deliberately done as part of its tax saving scheme in the form of disguised distribution of dividends designed to lessen its tax burden to the government.

We cannot subscribe to respondent's theory. The fact that petitioner was a-wholly-owned subsidiary of BOISE INTERNATIONAL, or that 99.24% of the capital stock of petitioner is owned by said BOISE INTERNATIONAL cannot be a sufficient basis to arrive at the conclusion that the interests due on the loans acquired are dividend distribution; and that it could not be said that there were no valid or bonafide loan transactions or true or bonafide indebtedness entered into between the parent company (BOISE INTERNATIONAL) and that of its subsidiary (BOISE CASCADE PHILIPPINES). In one American case entitled Van Clief et. a. vs. Helvering, Commissioner of Internal Revenue, No. 8351, April 12, 1943, 135 F2d 1417, 1419, United States Court of Appeals for the District of Columbia, ruled:

> "As stated above, we find nothing in the record to support the inference drawn by the Board that the advancements included in the $97,496.83 were not intended as a loans to the corporation and did not give rise to an indebtedness in that amount. This inference that a loan was intended is the natural and logical inference, and the fact that Van Clief was the sole stockholder of the corporation did not tend to rebut it. If the sole stockholder had been a corporation which made an advancement to its subsidiary, it would hardly be contended that the advancements did not give rise to an indebtedness as between themselves, although a claim on account thereof would have been postponed in bankcruptcy to the claims of other creditors. Sampsell v. Imperial Paper Co., 313 U.S., 215, 219 S. Ct. 904,85 L. Ed. 1293; IO

Ed. 1293; in re Smith 2 Cir., 36 F. 2d 697. There is no reason to apply a different rule because the sole stockholder is an individual. The fact that Van Clief made the advances to keep the corporation afloat rather than to liquidate it, has no tendency to show that a voluntary addition to capital rather than a loan was intended. See decisions of the Board in Harry T. Nicolai. Com'r, 42 B.T.A. 899, affirmed 9 Cir. 126 F. 2d 927; William D.P. Jarvis v. Com'r, 43 B.T.A. 439, affirmed Helvering v. Jarvis 4 Cir., 123 F., 2d 742; Edward Katzinger Co. v. Com'r 44 B.T.A. 533,536 xxx." (Underlining Supplied.)

It further said in the same case of Van Clief et al. v. Helvering, ibid, p. 1419, that the -

"xxx Advances are an additional contribution of capital if they are intended to enlarge the stock investment, but not if they are intended as a loan. Daniel Gimbel (v. Com'r), 36 B.T.A. 539; Bermuth-Lembecke Co. (v. Com'r), 17 B.T.A. 599; William D.P. Jarvis (v. Com'r), 43 B.T.A. 439. Here the parties intended the advances and loans. This is shown not only by the testimony of the officers, but by the entries on the book of the two companies are the consistent actions of the parties in regard to the advances, including their actions incident to the liquidation." (Underlining supplied.)

In determining whether a particular transaction can be considered a bonafide loan or a dividend distribution, the question is one of intention between the parties thereto as shown in the aforesaid transaction. This question of intention is a factual one to be decided from all the assembled circumstances. In one circumstance, where a promissory note was actually executed and an item of note receivable was carried in the books, this circumstance was considered in finding the existence of a loan. (Mertens, Law of Federal Income Taxation, Vol. 3, Chap. 9, pp. 70-72.) It is, therefore, the parties' intent, ascertained from all the relevant facts and circumstances, that is material in determining the true nature of the particular loan transaction. In distinguishing whether one is payment of dividends on stock, or the payment of interest on indebtedness, this was discussed clearly in a decision of U.S. District Court of Kansas, in the case of Associated Investors, Inc. vs. U.S. (52 AFTR 1210, 1213-1214), which we quote:

> The sole issue, as indicated by the stipulation, is whether the advancement to the corporation by its shareholders, for which were issued its promissory notes, represented a debt entitling it to deduct the designated interest on said notes from taxable income, or were contributions to capital and the payments were dividends or distribution of capital.
>
> This same question has been passed upon by the Court of Appeals for the Tenth Circuit, and this Court sees no particular reason for going beyond those decisions since they are binding upon this Court.
>
> What constitutes interest and what constitutes dividends are questions that have had the attention of the courts almost without limit.

In Crawford Drug Stores v. United States, 220F.2d 292, 295, Judge Bratton speaking for the court said:

> "* * * But in distinguishing between payment of dividends on stock and payment of interest on indebtedness the determining elements usually recognized for appropriate consideration are the name given to the certificates, the presence or absence of a maturity date, the source of the payments, the status of the holders in respect to being equal or inferior to that of regular corporate creditors, and the intention of the parties." (Emphasis supplied.)

This case is clearly distinguishable from the instant case as disclosed by the facts. The certificates in the Crawford Case were denominated perferred stock, payments were to be made only out of net earnings, on dissolution the rights of the holders were to be subordinate to the rights of ordinary creditors, the charter of the corporation provided for common and preferred stock, and the annual franchise returns reported shares of preferred as well as common stock. In the instant case the certificates were denominated promissory notes and they were so designated in the corporation tax returns. The minutes of the first meeting of the board of directors of the plaintiff corporation referred to the certificates to be issued as promissory notes, and in all of the corporation records, including its financial statements, the certificates were designated and treated as promissory notes. There was a fixed maturity date and the notes provided that interest should be payable semiannually. It was provided that the notes were to be treated on the same basis as claims of any other creditors of the corporation. In other words, the holders of these notes were to have no advantage whatever over common creditors, and the holder of any individual note was to receive no advantage over the holders of the other notes. The corporation unconditionally bound itself to pay a definite ascertainable sum regardless of earnings or surpluses, and the payment was not limited to the income of the corporation. There was nothing in the form of the promissory notes, their history and execution which indicated anything but a creditor relationship to the corporation, and under the stipulation, the holders of these notes treated them as promissory notes. Nor was there anything to indicate that they were to be treated as preferred stock or stock of any character.

In Bowersock Mills & Power Company v. Commissioner of Internal Revenue, 172 F.2d 904 /37 AFTR 960/, 907, the Court in an opinion by Judge Murrah stated:

> "* * * Although every case turns on its own facts, the courts have pointed out some of the indicia which mark the distinction between the debtor and creditor and stockholder relationship, such as the name given to the obligation; whether the holders have voting powers, and whether there is a fixed rate of interest. All of the courts agree that the most important, if not the controlling factor, is whether the obligation provides for certainty of payment of a fixed sum on definitely fixed dates."

And in the conclusion, although there existed preferred stock secured by a mortgage, the Court said:

> "When the whole transaction is viewed in the light of actualities, it is clear that the preferred stockholders remain creditors of the corporation, and that the payment on the obligation was deductible as interest."

Under the stipulation of facts, these stockholders holding the notes in question "advanced" to R.K. Stiles, as trustee, the sum of $25,000.00 to be used to purchase a designated 76-acre tract of land, which was sold at a sheriff's sale. After

> the trustee had received title to the property, then it was that he organized the corporation and these noteholders agreed to take their proportionate part of the issued stock and the promissory notes of the corporation for the remainder of the amount each "advanced."
>
> Certainly the entire transaction met the requirements of the Kansas statutes and the mere fact that this money was advanced for the purpose of enabling the immediate purchase of this land under the particular circumstances under which it was purchased, does not mean that those advancing the money were under obligation to take stock in the corporation for the full amount of their advancement. There is nothing irregular in the organization of the corporation and the fact that all of these notes were paid before the maturity date indicates that the corporate structure and the operation were in good faith.
>
> The most controlling element in determining whether the amounts in controversy are interests or dividends is the intention of the parties, i.e., the corporation and the noteholders. As hereinafter stated, in all of the proceedings of the corporation there appears the clear intention to treat that portion of the advancement made by each of the noteholders as a temporary loan rather than a definite contribution to capital.

To be more specific, in determining whether payment made are interests on indebtedness, hence deductible in the income tax returns, or disguished dividend distribution which is a capital item and is not deductible, <u>the real intention</u> of the parties must be sought and must turn upon the facts and circumstances surrounding each case. (Philippine Trust Co. vs. Comm., C.T.A. 367, Jan. 30, 1961; U.S. vs. Title Guarantee & Trust Co., 133 F 2d 990,993.) Where payments are made by a corporation on its shares of stock, these are dividends, but when the payments were made on evidence of indebtedness, these are interest payments and are deductible as expense. The intent of the parties are determined from all the facts and circumstances and once the intent of the parties becomes clear that controls. The characteristics of a loans are: a definite ascertainable obligation; a time of maturity, either definite or that will become definite. It may, of course, possessother features as well. (Par. 1902, PH. Fed. Tax Handbook, 1965) /Hotel Filipinas, Inc. vs. Comm., CTA. 1912, Nov. 26, 1971./

The question now for Us to determine is whether the circumstances and/or the factors in the abovequoted case of Associated Investors v. U.S., op cit., and the Hotel Filipinas, Inc. vs. Comm, op. cit., are present in the case at bar, so as to arrive at the conclusion that the said transaction is considered a bonafide loan. A close scrutiny of the records of this case reveals that substantial factors cited in the aforequoted cases are present in the case at bar concerning the transactions entered into between petitioner and BOISE INTERNATIONAL to bring us to the conclusion that they are more in the nature of interest income from loans than dividend distributions.

First, it is noted that the alleged loan investments were characterized by the existence of promissory notes. (see Exhibits F, pp. 25-26, BIR rec. Folder I; G and H, found in petitioner's envelope) While it may be true that the name given in an instrument may not be conclusive of its true nature, it is however a strong indication of the true intent of the parties in entering into a contracts of loan especially when other additional circumstances or factors, taken altogether are present. In this connection, Mertens (Law of Federal Income Taxation, Vol. 4A, Sec. 26.10, pp. 58-59) has this to say:

> "1. Did the parties intend at the time of the issuance of the original documents to create a debtor-creditor relationship? Both stocks and bonds evidence a contract between their holders and the issuing corporation; hence, in construing a contract the language used in reducing it to writing will normally be indicative of the intention of the parties.
>
> "2. Although not conclusive, what nomenclature and labels have been used? Interest is not changed into a dividend by merely calling it a dividend, and vice versa; likewise, a person who is a creditor is not changed into a stockholder by merely calling him one, and vice versa. Although, as stated, the name of an

> instrument is not conclusive as to its true character, the name given it may not be ignored, for the courts will not lightly assume that the parties have given to an instrument an incorrect name." (Underlining supplied.)

Second, the subject promissory notes have provided for the maturity dates of the loans' payments and their mode of payments, contrary to allegation of respondent. A close scrutiny of the first loan in the amount of ₱1,920,200.00, shows that it was covered by a promissory note of petitioner dated November 1, 1965 (Exh. G, found in petitioner's envelope) which provides that petitioner's payments of said loan should be made on or before September 1, 1970, with interest at 12% *per annum*. The second loan in the amount of ₱600,000.00, which is covered by a promissory note of petitioner dated November 6, 1965 (p. 35 BIR. rec. Folder II), provides that said petitioner shall pay the loan, at 12% interest *per annum*, within thirty days from date of demand. The third and last loan, in the amount of ₱11,400,000.00, evidenced by a promissory note of petitioner dated January 3, 1967 (Exh. F, pp. 25-26, BIR rec. Folder I), provides that said petitioner shall pay the same within one year after demand, with interest at 8 3/4% *per annum*. Definitely, there is a definite time frame in which the interests on the various loans of petitioner should be paid to its principal the BOISE INTERNATIONAL.

Again, these factors will definitely show that there exist a situation of creditor and debtor relationship because the promissory notes provide for payment of a definite sum and a fixed time to repay the same. In this connection, Mertens (op. cit., pp. 60-61) again, has this to say:

> "Does the obligation have a definite maturity date fixed or ascertainable? That feature is ordinarily the essential element of a creditor investment. The fact that ultimately there must be paid a definite sum at a fixed time marks the relationship to the corporation as that of creditor rather than shareholder." (Italics ours.)

It is to be noted that petitioner, under the said promissory notes executed in favor of BOISE INTERNATIONAL are payable unconditionally to the latter regardless of whether there is or there is no profit or surplus. These categorical and unconditional obligation of petitioner, under the said promissory notes, clearly establishes the existence of a creditor and debtor relationship, i.e. between petitioner, as debtor, BOISE INTERNATIONAL, as creditor. In the instant case, the alleged advances made by the BOISE INTERNATIONAL to petitioner supports strongly a finding which we so hold that said alleged amounts of advances are considered rightly and legally as loans. Again, to this holding, Mertens (ibid., p. 65) says as follows:

> Is the obligation to pay positive and unconditional or subject to a contingency? The fact that funds were advanced with reasonable expectation of repayment supports a finding that the advances were loans. Ordinarily, indebtedness is founded upon a positive obligation to pay. The creditor must be entitled in all events to the return of the money loaned. The shareholder is entitled to nothing prior to liquidation, except out of earnings. The creditor is entitled to payment of interest and principal from the corpus of a debtor's property, regardless of whether there is a surplus of earnings. In compensation for not sharing the profits, the creditor is to be paid independently of the risk of success. This distinction marks a vital difference between the shareholder and the creditor. (Underlining supplied.)

Third, the said loans were approved by the Central Bank as foreign loans. Central Bank Circular No. 289 provides that existing foreign obligations, not registered with the Central Bank before November 26, 1969, shall not be allowed the remittances of interest abroad, except only upon the registration and approval of the loans by the Central Bank. Petitioner, in compliance with aforesaid requirements, had submitted all its promissory notes and supporting papers to the Foreign

Exchange Department of the Central Bank and after a thorough verification, the latter accepted and registered the same as foreign loans. (see Exhs. I and J, found on petitioner's big envelope.) The approval of said promissory notes and their consideration as foreign loans by the Central Bank is a clear indication of the true nature of the said transactions, which is a distinct factor showing the existence of the relationship of BOISE INTERNATIONAL as creditor and that of petitioner the BOISE PHILIPPINES, as debtor.

Fourth, the aforesaid loans were all considered and treated by petitioner in its corporate books and financial statements as loans and liabilities, (T.S.N. p. 117, Oct. 2, 1980; see also Ibid. pp. 18-23, April 11, 1980; Exhs. N, N-1-a, O, O-1-a, P, P-1-a) Interest payments were likewise reflected in petitioner's books of account (TSN. p. 17, April 11, 1980). This treatment of the transactions is a factor again indicative of the existence of creditor and debtor relationship between petitioner and that of BOISE INTERNATIONAL.

Fifth and lastly, the said loans secured by petitioner from the BOISE INTERNATIONAL were ultimately paid. In accordance with the terms of the promissory notes, the aforesaid loans were later finally paid by petitioner. The balance sheet for the year ended 1973 of petitioner shows that there exists no more liability of petitioner from the BOISE INTERNATIONAL arising from said loans. As testified to by petitioner's witness, Mrs. Luz Bitong, the loan in the amount of ₱600,000.00 was paid in 1970; the ₱1,920,200.00 loan was paid in 1971; and the ₱11,400,000.00 was paid in 1972.(TSN. pp. 75-77, August 11, 1980; see Exh. O-1-a).

Considering all these above factors, and taken altogether, it points to no other conclusion than that there exists in truth, in fact, and in law, a creditor-debtor relationship between petitioner and the BOISE INTERNATIONAL and, hence, the accrued interests claimed by petitioner as expense deductions in its income tax returns, are valid and legal and are deductible.

We will now dispose of the second issue as to whether or not respondent's right to assess petitioner for the fiscal year ended June 30, 1966 has already prescribed.

Petitioner contends that the amended income tax return for 1966 was filed by it on January 12, 1967. However, the demand or assessment letter which was dated

April 3, 1972 (Exh. C, pp. 194-196 BIR rec. Folder I) was released by respondent on April 12, 1972 (Exh. C-1, p. 194, BIR rec. Folder I), which date of release of the assessment is five years and three months counted from the date of filing of the petitioner's income tax return for 1966. Therefore, petitioner concluded that the right of respondent to assess petitioner's deficiency income tax for said year 1966 has already prescribed pursuant to Section 331 of the 1972 Tax Code and there was no valid waiver of the statute of limitation signed by the Commissioner of Internal Revenue which may suspend the running of the period of prescription.

On the other hand, respondent contends that the assessment in question was filed within the prescribed period because petitioner had executed and signed a waiver of statute of limitation under Section 332(b) of the National Internal Revenue Code and said waiver was signed by the Revenue District Officer of Makati.

The main point therefore to be determined is whether or not there was a proper filing of a valid waiver of the statute of limitation which was actually signed by petitioner and Revenue District Officer in pursuance to

Section 332(b) (now Sec. 319) of the Tax Code, which reads as follows:

> SEC. 332. Exceptions as to period of limitation of assessment and collection of taxes. -
>
> xxx xxx xxx
>
> (b) Where before the expiration of the time prescribed in the preceding section for the assessment of the tax, both the Commissioner of Internal Revenue and the taxpayer have consented in writing to its assessment after such time, the tax may be assessed at any time prior to the expiration of the period agreed upon. The period so agreed upon may be extended by subsequent agreements in writing made before the expiration of the period previously agreed upon. (Underlining supplied.)

The law is clear and explicit that a valid waiver of the statute of limitation provided for in the above-quoted provision of the law requires that the said statute of limitation must be in writing and must be both signed by the Commissioner of Internal Revenue and the taxpayer. A close scrutiny of the aforesaid waiver of the statute of limitation (Exh. L., p. 173, BIR rec., Folder I) shows that Revenue District Officer Sixto J. Javier had merely attested the aforesaid waiver; that aforesaid officer did not sign the waiver either for or by virtue of the authority of the Commissioner of Internal Revenue. Clearly, for all legal intents and purposes of the above law, Section 332 of the National Internal Revenue Code, there was no valid waiver executed by herein Commissioner of Internal Revenue and petitioner to stop the running of the period within which to validly assess the tax in question.

In the instant case, the language of said statute of limitation being plain and unambiguous, it conveys a clear and definite meaning, and, therefore, said statute must simply be applied and never to be interpreted.

> 225. Dependence of Construction upon Ambiguity. - A statute is not open to construction as a matter of course. It is open to construction only where the language used in the statute requires interpretation, that is, where the statute is ambiguous, or will bear two or more constructions, or is of such doubtful or obscure meaning, that reasonable minds might be uncertain or disagree as to its meaning. Where the language of a statute is plain and unambiguous and conveys a clear and definite meaning, there is no occasion for resorting to the rules of statutory interpretation, and the court has no right to look for or impose another meaning. In the case of such unambiguity, it is the established policy of the courts to regard the statute as meaning what it says, and to avoid giving it any other construction than that which its words demand. The plain and obvious meaning of the language used is not only the safest guide to follow in construing it, but it has been presumed conclusively that the clear and explicit terms of a statute expresses the legislative intention, so that such plain and obvious provisions must constrol. A plain and unambiguous statute is to be applied, and not interpreted, since such a statute speaks for itself,

> and any attempt to make it clearer is a vain labor and tends only to obscurity. xxx xxx. (Am. Jur., Vol. 50, 1944 Ed., pp. 204-207.)

In the case at bar, the law is clear and definite that it is only the Commissioner of Internal Revenue, who is specially named by said provision of Section 332(b) of the Tax Code, as the one who can sign the waiver of the statute of limitation, and since the Commissioner has not signed the waiver, there is, therefore, no consummated or valid waiver which may suspend the running of the period within which to assess the tax in question. (Coll. vs. Solano, GRL-11475, July 31, 1958, p. 6.) Consequently, respondent's assessment which was made more than five years from the filing of petitioner's amended income tax return on January 12, 1967 for the taxable year 1966 has prescribed.

We will now consider the third issue as to whether or not petitioner has already paid the withholding taxes in question. Respondent admits that there were indeed payments made by petitioner, but such payments were actually payments for other taxable years and not for the period covered by the assessment in question.

A close scrutiny of payments made by the petitioner as shown in the exhibits presented, and which corroborate the testimony of petitioner's witness Luz Bitong, will bring out the fact that there were different amounts of interest income remitted which show the dates of remittances and the amounts of income taxes withheld therefrom and which were and actually paid.(T.S.N., pp. 45-66, May 27, 1980; Exhs. AA, BB, CC, and DD found in petitioner's envelope.) Petitioner was able to establish by sufficient evidence through the efforts of Luz Bitong, who verified the amounts of interests which accrued during the years in question, and which tallied with those appearing in petitioner's books of account. The withholding taxes were also tallied, and except in the difference of tax rates of withholding tax applied, which is 30% by respondent for years 1966, 1967 and 1968, while petitioner had computed, applied and paid the correct 35% withholding taxes in the years 1970, 1971 and 1972. (see TSN., pp. 59-65, May 27, 1980; also see Exhs. AA, BB, CC and DD, in petitioner's big envelope). It is noted further that the former Deputy Commissioner Conrado Diaz issued a memorandum to the effect that a verification from respondent's Accounting Division showed that petitioner paid more than two million pesos in withholding taxes. (see Exh. R, p. 300, BIR rec. FolderII).

Respondent, on the other hand, had failed to present evidence rebutting the evidence presented by petitioner which to Us are satisfactory and convincing. The Court is therefore of the opinion and so hold that the withholding taxes assessed against petitioner in this case had already been paid.

Anent the fourth issue, the question to be resolved is whether or not the obligation to withhold and pay the income tax at source should be based upon accruals of the interest income or upon remittance thereof to the foreign corporation BOISE INTERNATIONAL.

Respondent contends that for tax purposes, whenever interest incomes are due to a foreign corporation not engage in trade or business in the Philippines, like the BOISE INTERNATIONAL, the liability of the taxpayer to withhold and pay the income taxes due to the government on the interest income should be at the time of the accrual of said interest income in petitioner's books of account, and not at the time of the actual remittance or payment thereof to the recipient foreign corporation, and even though the amount of interest incomes cannot be remitted due to or/on account of Central Bank restriction; and that the said rule should be enforced as if there is no restriction at all pursuant to the BIR Ruling 71-003 dated February 26, 1971.

Petitioner, on the other hand, strongly contends that the obligation to withhold and pay taxes at source should be on the dates of actual remittance or payment of the interest incomes and which cannot be made at the time of accrual since such interest incomes cannot be remittable because of Central Bank restrictions. We concur with the petitioner. This issue is no longer one of first impression. In the case of Bayer Pharmaceuticals, Inc., vs. Commissioner of Internal Revenue, CTA Case No. 2846, March 16, 1979, decided by this court, it was held as follows:

> The lone question tendered for resolution is whether or not the obligation to withhold and pay income tax-at-source on the royalties is upon the accrual of the royalties or upon the actual remittance or payment thereof.
>
> Petitioner maintains that there was no obligation to deduct, withhold, and pay the withholding tax in 1972 since the royalties could not be remitted due to Central Bank restrictions. In submitting, however, that the liability to withhold and pay the income tax withheld at source from royalty payments to a non-resident foreign corporation, like Bayer Aktiengesellschaft, Leverkusen Bayermerk, is at the time of the accrual of said royalties and not at the time of the actual remittance or payment thereof, respondent relies mainly on Bureau of Internal Revenue Ruling No. 71-003, dated February 26, 1971, the pertinent portions of which are quoted as follows:
>
>> "This refers to your letter dated February 16, 1971 requesting a ruling as to the basis of the withholding tax due on film rentals or royalties payable by you to non-resident foreign film corporations.
>>
>> "xxx xxx xxx

"In your letter, you contended that the 35% withholding tax should be based only on actually remittable amount under Central Bank regulations and not on the entire amount due and payable to the non-resident foreign corporation. This contention has no legal basis. Withholding tax is not dependent on remittance of the income payable to the non-resident foreign corporation but on accrual thereof. Such being the case, although a portion of the amount due to the non-resident foreign corporation cannot be remitted on account of Central Bank restrictions, the tax due on said portion should be deducted and withheld as if there is no restriction.

> 'Restricted funds.- In connection with the restriction on the transfer of funds from U.S. to persons in Norway, Denmark, the Netherlands, Belgium, Luxembourg and France, the tax should be withheld in the same manner as if no restriction existed. In custodian accounts, the name of the foreign bank or other foreign person should be entered on the ownership certificate, and an amended ownership certificate filed as soon as the actual owner is disclosed.' (CCH, 1969, Vol. 5, par. 4875.405)

"In view thereof, this Office believes and so holds that the 35% withholding tax should be deducted and withheld on the entire amount of film rentals or royalties payable to the non-resident foreign film corporations including that portion which, on account of Central Bank restrictions, cannot as yet be remitted abroad."

As expressly stated therein, the Bureau of Internal Revenue ruled that withholding tax is not dependent on remittance of the income payable to the non-resident foreign corporation but on accrual thereof. And as such, although the income cannot be remitted on account of Central Bank restrictions, the tax due thereon should be deducted and withheld as if there is no restriction.

The statute involved is Section 53(b)(2) of the National Internal Revenue Code, the controlling provisions of which read as follows:

> "Sec. 53(b)(2) Non-resident foreign corporations. - In the case of foreign corporations subject to tax under this Title, not engaged in trade or business within the Philippines, there shall be deducted and withheld at the source in the same manner and upon the same items as is provided in Subsection (b)(1) of this section, x x x x, a tax equal to 35 per cent thereof. This shall be returned and paid in the same manner and subject to the same conditions as provided in Section 54. x x x x"

And Section 53(b)(1) of the same Code pertinently provides:

> (b) Non-resident aliens and foreign corporations. - (1) Non-resident aliens. - Every individual, corporation, partnership, or association, in whatever capacity acting, including a lessee or mortgagor of real or personal property, trustee acting in any trust capacity, executor, administrator, receiver, conservator, fiduciary, employer, and every officer or employee of the Government of the Republic of the Philippines having the control, receipt, custody, disposal, or payment of interest dividends, rents, royalties, salaries, wages, premiums, annuities, compensation, remunerations, emoluments, or other fixed or determinable annual, periodical, or casual gains, profits, and income, and capital gains, of any non-resident alien not engaged in trade or business within the Philippines, shall (except in the

cases provided in sub-section (a)(1) of this Section) deduct and withhold from the annual, periodical, or casual gains, profits, and income, and capital gains, a tax equal to 30% thereof.

x x x x x

These provisions, by the way, were merely imported and copied almost verbatim from similar withholding tax provisions of the United States Revenue Code /Section 143(b)/. Accordingly, in consonance with settled rules of statutory construction, the interpretation they have received in the United States have authoritative effect in the proper construction and interpretation of our law.

Thus, as correctly noted by petitioner and which is not disputed by respondent:

1. In arriving at BIR Ruling No. 71-003, dated February 26, 1971, our Bureau of Internal Revenue quoted as authority the excerpt of a United States Internal Revenue Service ruling which is found at par. 4875.405 of CCH, 1969, Volume 5. It appears that the said U.S. ruling is actually Mimeograph Ruling No. 5075, which was issued by the Office of the Commissioner of Internal Revenue, Washington, D.C. on July 8, 1940 and can be found at the Cumulative Bulletin 1940-2, at page 141.

2. The said Mimeograph Ruling No. 5075 has been declared obsolete by the United States Internal Revenue Service itself in its Revenue Ruling No. 70-293. (U.S. Internal Revenue Bulletin No. 1970-23, dated June 8, 1970) It is thus evident that in issuing its BIR Ruling No. 71-003 on February 26, 1971, our own Bureau of Internal Revenue has relied on a United States Internal Revenue Service ruling that has already been overruled, the same having been declared obsolete as of June, 1970.

3. Following the decision of the United States District Court in L.D. Caulk Co. vs.

United States, 116 F. Supp. 835, rendered on November 19, 1953, to the effect that corporation which held licenses under patents owned by non-resident aliens who as result of blocking proclamation were forbidden right to receive or dispose of royalties was not bound to withhold tax before payment of royalties, the rule that is now observed in the United States is that the obligation to withhold and pay the tax is upon payment or remittance of the income to a non-resident alien.

In the L.D. Caulk Co. case, where the factual setting, law involved and issue litigated are practically on all fours with the case at bar, plaintiff, a Delaware corporation, held licenses under patents owned by two non-resident aliens, Robert Doge and Emmanuel de Trey. Both patentees were Swiss. Under the licensing agreements, plaintiff obligated itself to pay royalties to Doge and de Trey. In its treatment of the impact of royalties on its operations, plaintiff, adhering to the accrual method of accounting, entered net royalties and withheld taxes as accrued liabilities of 1941 and 1942, the periods involved in the case. Thus, 1941 and 1942 royalties and taxes were set up as accounts payable on plaintiff's books and as part of its cost of doing business for those years. No withholding returns for non-resident aliens Doge and de Trey were prepared for 1941 or 1942. While the critical issue is when the returns wer due for royalties attributable to sales made by plaintiff during the years 1941 and 1942, the inquiry shifted from "when was the return due" to "when, if at all, was plaintiff required to withhold the tax from the royalties." There was no question raised by plaintiff as to existence of its duty to withhold on the royalties. The "when" of the matter, not the "who" or the "what" was the point of dispute and inquiry because, as result of blocking proclamation, non-resident aliens were forbidden right to receive or dispose of royalties due them under contract with corporation which held licenses under aliens' patents. (L.D. Caulk Co. vs. United States, 116 F. 835, 840.) Stated otherwise, the question as to when to withhold the tax from the 1941 and 1942 royalties arose because, although the royalties were accrued in the plaintiff's books in 1941 and 1942 as liability to the non-resident licensors, the same could not be paid or remitted to the latter as a result of a blocking proclamation.

The United States Federal Court ruled that where, as result of blocking proclamation, non-resident aliens were forbidden right to receive or dispose of royalties due them under contract with corporation which held licenses under aliens' patents, such aliens had no "gains, profits and income" within internal revenue statute requiring all persons having control, receipt, custody, disposal or payment of fixed or determinable annual or periodical gains, profits, and income of any non-resident alien to withhold tax and, therefore, no necessity of filing withholding tax return devolved on corporation while corporation retained blocked royalties. The net result is that the obligation to withhold and pay the tax is upon payment or remittance of the United States derived income to the non-resident recipient. Because of its strong persuasive force, if not controlling effects, on the present case, we will quote at length from the decision.

> "The onus of the withholding requirement on plaintiff is imposed by § 143(b), I.R.C.: "All persons, in whatever capacity acting, * * * having the control, receipt, custody, disposal, or payment of * * * fixed or determinable annual or periodical gains, profits, and income * * * of any nonresident alien * * * shall deduct and withhold from such annual or periodical gains, profits, and income a tax * *." On the whole, this provision does not concern itself with "when" the withholding should take place. Rather, it simply specifies "who" shall do "what". However, this much light it does shed. The duty to withhold presupposes the existence of "annual or periodical gains, profits, and income". The section directs the withholding from such sums as are identifiable as "gains, profits, and income" of the nonresident alien. Obviously,

if there are no such "gains, profits, and income", the duty to withhold is nonexistent. On the other hand, if there are such sums available, the statutory language is inconclusive in deciding "when" the withholding duty arose.

I do not ground my decision on any subtlety of construction, but I do advert, in fact, to it. Were the royalties "gains, profits, and income" to the aliens Doge and de Trey while plaintiff retained them under these circumstances? I think not upon a realistic view of the matter. The blocking proclamation plucked every element of control over the funds from the alien's theoretical bundle of ownership rights. This loss of the essence of private ownership occurred while the royalties were still in plaintiff's possession, since the blocking freeze applied to individual debtors of Swiss nationals. As soon as royalties accrued to the aliens under the contract, this crazy predicament faced them: they had theoretical right to collect the royalties but were forbidden right to receive them or dispose of them. No economic advantage was theirs. Such a hollow "right" does not have the core of benefit sufficient to constitute "gains, profits, and income". Even the ubiquitous doctrine of constructive receipt of income has no tentacle long enough to reach these royalties. Cf Reg. 103, § 19-42-2. As said with reference to § 22-(b)(2), I.R.C., in Industrial Trust Co. v. Broderick, 1 Cir., 94 F.2d 927, at page 930, "Throughout the Revenue Laws the words gain, profit, or income mean an actual, not a fictitious gain or profit * * *." Certainly, these were not "income" and, if "gains, or profit", were unrealized and highly artificial. Further, the aliens here had no power to command payment to themselves or others, unlike

> the donor of the interest coupons in Helvering v. Horst, 311 U.S. 112, at page 118, 118, 61 S.Ct. 144, 147, 85 L.Ed. 75, where it is said: "The power to dispose of income is the equivalent of ownership of it." It would seem, then, there being no 'gains, profits, or income" of the aliens at least during the time plaintiff retained their blocked royalties, no withholding duty devolved on plaintiff and no penalties are proper."

Against this backdrop, the situation here presented, while the royalty in the amount of ₱69,529.00 (although was set up in the books of petitioner as a liability to Bayer) could not be remitted to Bayer due to Central Bank restrictions at that time, would not create "gains, profits or income" to non-resident foreign corporation Bayer. No economic benefits were derived by Bayer; hence, there was no income subject to withholding of tax-at-source. Accordingly, petitioner had no duty to withhold and pay the tax.

Even more, adopted basis for the decision of the United States Court is the legislative history of Section 143(b) of United States Tax Code, from which Section 53(b) of our National Internal Revenue Code was practically copied, and hints derived from the published pronouncements of the United States Bureau of Internal Revenue and Courts, which disclose that duty of withholding arises at time of payment. We quote from L. D. Caulk:

> "Present § 143(b), I.R.C., is traced back to the Act of October 3, 1913. Paragraphs D and E of that Act are pertinent. Paragraph D provided: "* * * all persons * * * having the control, receipt, disposal, or payment of fixed or determinable annual or periodical gains, profits, and income of another person subject to tax, shall in behalf of such person deduct and withhold from the payment an amount equivalent to the normal income

tax * * *." Paragraph E of the same Act in part specified: "All persons * * * having the control, receipt, custody, disposal, or payment of * * * other fixed or determinable annual gains, profits, and income of another person, exceeding $3,000 for any taxable year * * * who are required to make and render a return in behalf of another, as provided herein, * * * are hereby authorized and required to deduct and withhold from such annual gains, profits, and income such sum as will be sufficient to pay the normal tax * * * and they are each hereby made personally liable for such tax." Paragraph D is explicit in directing withholding from the "payment" while its companion section authorizes the deduction and imposes personal liability on the withholding agent. In its Report to the House of Representatives on the Bill, the Committee on Ways and Means said, "Probably two-thirds of the income tax proposed as to individuals would be deducted and withheld at the source of the income and paid in full to the Government. * * * By this method the amount of tax due or to become due upon every fixed or determinable annual income is withheld and paid to the Government before the income reaches the taxpayer". Nonresident aliens as well as citizens were subject to this withholding system.

In the 1916 Act, quoted paragraph D was repeated as section 8(d) under the significant heading "Returns". Paragraph E, as quoted, was repeated as section 9(b) under the heading "Assessment and Administration".

By the Revenue Act of 1917, paragraph 8(d) of the 1916 Act (par. D of the 1913 Act) was repealed so as to render unnecessary any "withholding at the source of the tax due on profits or incomes of resident taxable persons". Information at the source was substituted. According to the House Report, this change was made for "a more effective administration of the law" and the "saving of annoyance and expense to the taxpayers and withholding agents". By the same Act, paragraph 9(b) of the 1916 Act (par. E of the 1913 Act) was amended to limit withholding at the source to nonresident aliens. The Act further included interest from tax-free covenant bonds as a subject of withholding.

The Revenue Act of 1918 made no change in the pertinent language of the amended § 9(b) but did increase the withholding rate and renumbered the section as 221. However, the Report of the Ways and Means Committee of the House aids search in its comments on "Collection at the Source": "The proposed bill, as under existing law, requires only the withholding of income in the case of payments by individuals, corporations, and partnerships of fixed and determinable annual or periodical gains, profits, and income to nonresident alien individuals or nonresident corporations". This comment is an indication the intent of Congress was as expressed in paragraph D of the 1913 Act and was continued in § 9(b) of the 1917 Act when the former provision was repealed. No change was intended when the withholding provisions were delimited to apply only to nonresident aliens. The time of payment was the time when the withholding duty arose.

The Revenue Act of 1921 made no amendments to the Section pertinent to inquiry, nor did the Act of 1924. However, both the House Report and the Senate Report on the 1924 Act have this comment: "Section 221: Subdivision (a) of this section of the present law provides for the withholding of a tax, equal to the normal tax, on fixed or determinable income paid to a nonresident alien individual, or a partnership composed in whole or in part of nonresident aliens." Both also refer to "requiring the withholding of tax from payments" to a partnership.

Rates of withholding were increased by the Revenue Act of 1926, and the Conference Report of the Committees of the House and Senate refers to the effect of the hike in rates: "This amendment requires the withholding of a tax of 12½ per cent in respect of all payments of income made before the enactment of this Act and 13½ per cent in respect of such payments made after the enactment of this Act to foreign corporations specified below. * * * Because the persons making payments * * * had no notice that the corporation income tax would be increased, the withholding rate is not increased with respect to payments made before the enactment of this Act; * * *". Although reference is to foreign corporations, the withholding on payments to them is but a part of the same system embracing individuals.

In the Revenue Act of 1928 a wholesale departure was made from the arrangement of prior Acts. § 221 became § 144. In commenting on part (a) of the Section, both the House Report and the Senate Report stated: "The present law provides for the withholding at the source, in the case of bonds, of a tax of 5 per cent of the interest when paid to nonresident aliens. * * *."

Under the Revenue Act of 1932, the section was renumbered 143 and the rates were increased without affecting the aspect of the provision under consideration.

The Revenue Act of 1934 made no changes bearing upon our inquiry, but again in the House Report and in Senate Report references to withholding of tax on interest obligations were couched in terms of payment.

The 1936 Act did not change the terms of § 143 as they affect the problem under investigation. However, a comment in the Senate Report confirms the prior statements: "Section 32 of the existing law provides that the tax withheld at the source under section 143 from payments to an individual taxpayer shall be acredit against such taxpayer's tax". Reference is also made to "withholding in the case of payments to foreign corporations".

The House Report, which the Senate adopted, on the Revenue Act of 1937 is equivocal in stating with reference to a change in § 211(a): "There will be withheld from the amounts receivable by a nonresident alien taxed under the new provisions the amounts required to be withheld under section 143 of the present law". "Receivable", of course, is descriptive of minute divisions of time from the first moment of accrual to the last second before receipt of payment.

The House Report on the Revenue Act of 1938 appears to reaffirm the earlier interpretations even if the 1937 Report be viewed as a deviation. In referring to consent dividends, the Committee on Ways and Means reported: "In case any shareholder making a consent is a person subject to the provisions of section 143 (b) and section 144, relating to the deduction and withholding of tax at the source, section 28(d)5 requires that such consent filed by the corporation with its return shall be accompanied by cash * * * equal to the amount which the corporation would have been required to deduct and withhold by such section 143 (b) or 144 if the amount specified in such consent had been paid to such shareholder, on the last day of the taxable year of the corporation, in cash as a taxable dividend." The Senate Report used same language in referring to § 143(b).

No pertinent comment was found in the Committee Reports on the other Revenue Acts down to 1941 and 1942, the tax years in question. However, one further reference is made to a later committee report reflecting current thinking. The House Report on the Revenue Act of 1950 in referring to a proposed § 1311(a) states: "This subsection also provides that any person required to deduct and withhold a tax under section 143 or 144 * * * on the payment of a dividend shall not be required to deduct and withhold a tax under this section upon such payment".

Regulations promulgated by the Commissioner contain abundant references to payment as indicating the crystallization of the withholding duty. Treasury Regulations 111, § 29.143-1(a) states: "Withholding of a tax of 30 percent * * * is required in the case of fixed or determinable annual or periodical income paid to a nonresident alien individual * * *". The subsections of § 29.143 are replete with references to withholding upon payment, such as "The tax must be withheld at the source from the gross amount of any distribution made by a corporation" (29.143-1); "* * * an annual return * * * showing the amount of tax required to be withheld from each nonresident alien * * * to which income other than interest was paid during the previous taxable year" (29.143-7); "Tax withheld at the source upon * * * income paid to nonresident alien fiduciaries * * *" (29.143-9).

And even on the question of whether withholding should be at the rate in effect at the time payments were <u>due</u> or at the rate when payments were actually <u>made</u>, the United States Court ruled that the time payment is <u>made</u> governs the rate. We again quote from the <u>Caulk</u> decision:

"On the issue of whether withholding should be at the rate in effect at the time payments were due or at the rate when payments were actually made, the Bureau has ruled the time of payment governs the rate. O.D. 167, 1 C.B. 192; I.T. 1521, I-2 C.B. 197; I.T. 3020, XV-2, C.B. 106; I.T. 3291, 1939-1, C.B. 140. Cf. I.T. 3535, 1942-1, C.B. 129; I.T. 3342, 1940-1, C.B. 58. In fact, language sufficiently broad to encompass the problem was employed in G.C.M. 2467, 7-2 C.B. 138 (modified on other grounds in G.C.M. 8594, 9-1 C.B. 354): "* * * withholding is only required when * * * income is paid to a nonresident alien and at the rate in force at the time of payment."

As in the above, so Southern Pacific Railroad Co. v. C.I.R., 21 B.T.A. 990, held rate of withholding was that which was effective on the date of actual payment. In that case, the petitioning company contented unsuccessfully for a result similar to the one here sought by

> the Government. Bond interest due and payable during 1914-1917 could not then be paid to nonresident aliens because of war restrictions. It was, in fact, paid in 1921 and 1923, after the withholding rates had been increased. The company argued the former, lower rates should apply because the interest was then due; sufficient funds were available at all times for its payment; and the date of constructive receipt by the bondholders gave rise to the duty of withholding. The Board of Tax Appeals rejected these arguments, saying, 21 B.T.A. at pages 995 and 996: "The petitioners did not and were not called upon to pay the interest until 1923, and the nonresident aliens did not and for all that appears could not receive the interest until then * * *. When the interest was actually paid to and received by the bondholders they received income taxable at the rate then effective, and the petitioners were under the duty of paying so much thereof as by the statute then in effect they were required to withhold and pay." Oblique support is thus given to adoption of the time of payment as the maturation point of the withholding duty, payment being both an easily recognizable act of objective significance and a standard safeguarding the collection of the proper amount of tax."

What possible ground can there be for us not to apply to petitioner the ruling of the United States Federal Court in L.D. Caulk, supra, for which Bayer Pharmaceuticals, Inc., is similarly situated? A decision buttressed by the law, which is closely if not exactly similar to our law, reason and logic is not to be simply brushed aside to accommodate a ruling of our own Bureau of Internal Revenue which merely quoted as authority the excerpt of a United States Internal Revenue ruling but which excerpt has been declared obsolete by the same United States Internal Revenue Service as a result of the L.D. Caulk decision. As we view this legal problem, we find no cogent and valid reason to modify, much less depart from the conclusion reached in L.D. Caulk, as expressed in the above-quoted opinion of the United States Court there, and the same should resolve the identical issue now brought before us in this proceeding. We cannot ignore the well-settled principle of construction that since our income tax law was practically copied from that of the United States, the interpretations it has received in the United States have authoritative effect in the proper construction and application of our law. More so in the case of our withholding tax-at-source provision embodied in Section 53(b) of our National Internal Revenue Code which, as shown above, was merely imported and copied almost verbatim from Section 143(b) of the United States Tax Code during the year involved in the L.D. Caulk decision. Accordingly, the conclusion reached in L.D. Caulk, which is followed by the United States Internal Revenue Service - that the time of payment of the royalties is the maturation point of the withholding duty - should govern this proceeding.

Not much need be said on respondent's assertion that, based on the report of the investigating examiner, nothing is stated that petitioner attempted to remit the royalties to Bayer. By respondent's own decision, it is explicitly declared "that the royalties in the amount of ₱69,529.00 were not remitted by BPI (petitioner herein) to Bayer due to Central Bank restrictions." (Exh. "5," Exh. "E-1," p. 30, BIR records) Since the royalties could not be remitted to Bayer due to Central Bank restrictions, as stated by respondent himself in his decision appealed from, surely, respondent's counsel should not expect petitioner to make efforts, albeit unlawful, to remit the same. And on respondent's point that since the royalties had been accrued in petitioner's books the income thereon became subject to with-

> holding even if remittance was effected later, suffice it to say that the accrual of the royalties in petitioner's books, as held in the L.D. Caulk, did not amount to "gains, profits and income" on the part of non-resident Bayer and, therefore, no necessity to withhold tax devolved on petitioner.
>
> We, accordingly, rule that since the royalties in question could not be paid or remitted in 1972 by petitioner Bayer Pharmaceuticals, Inc., to non-resident foreign corporation Bayer Aktiengesellschaift, Leverkusen Bayermerk due to Central Bank restrictions, petitioner was under no obligation to withhold and pay income tax-at-source on said royalties and, therefore, it is not liable for the deficiency withholding tax-at-source assessment of respondent Commissioner of Internal Revenue x x x". (Appeal denied in Bayer Pharm., Inc. vs. Comm. of Int. Rev., GR L-72054, on Sept. 29, 1986.)

We will now consider the final and last issue as to whether or not 25% surcharge, interests and compromise penalty are imposable on the petitioner.

The 25% surcharge, as provided in Section 72 of the Tax Code, is imposed in case of failure to file a return within the time prescribed by law and which failure to file was not due to willful neglect. In the case at bar, there exists no failure on the part of the petitioner in filing its required returns. It is sufficiently established by evidence that petitioner paid and remitted the interests due on the loans secured during the years 1970, 1971 and 1972 and it was only during these said years that petitioner was required to and did in fact filed the corresponding returns. (Exhs. EE, EE-1, FF, FF-1, FF-2, GG, GG-1 and GG-2, found on petitioner's big envelope). As we have said heretofore, the obligations to withhold and pay the corresponding withholding tax arises only upon the actual payment or remittance of the interest income to the non-resident foreign taxpayer, in pursuance to the doctrine laid down in the case of Bayer Pharmaceuticals Inc. vs. Commissioner of Internal Revenue case aforesaid.

Besides, petitioner filed its returns voluntarily without previous notice or order to do so by the respondent; for which reason, the filing of the returns by petitioner can not be said to be due to a willful or intentional neglect with the intention to evade payment of income tax. Therefore, no such 25% surcharge is imposable under Section 72 of the Tax Code.

The deficiency interests should not also be imposed inasmuch as petitioner is not liable for deficiency income tax and withholding income tax as previously found by Us.

Equally so, the compromise penalty is likewise not imposable. It is enough to state that a compromise penalty cannot be imposed by respondent Commissioner of Internal Revenue without petitioner's conformity thereto. (Phil. Int. Fair Inc. vs. Coll. of Int. Revenue, 4 SCRA, 774, 781-782; Coll. of Int. Rev. vs. University of Sto. Tomas et. al., G.R. No. L-11274 and L-1128, November 28, 1958; Rizal Motors Inc. vs. Comm. of Int. Rev., C.T.A. Case No. 1985, December 27, 1972; Liberty Insurance Corporation vs. Comm. of Int. Rev., C.T.A. Cases Nos. 3551 & 3599, Oct. 15, 1986.)

WHEREFORE, the decisions of the Commissioner of Internal Revenue appealed from dated January 25, 1977 and January 28, 1977 are hereby accordingly reversed and set aside.

No pronouncement as to costs.

SO ORDERED.

Quezon City, Metro Manila, March 30, 1987.

CONSTANTE C. ROAQUIN
Associate Judge

WE CONCUR:

AMANTE FILLER
Presiding Judge

ALEX Z. REYES
Associate Judge