Republic of the Philippines
COURT OF TAX APPEALS
Quezon City

SECOND DIVISION

MIRANT (PHILIPPINES) ENERGY CORPORATION,
Petitioner,

- versus -

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

C.T.A. CASE NO. 6561

Members:

Castañeda, Jr., *Chairman*
Uy, and
Palanca-Enriquez, JJ.

Promulgated:

JUN 17 2005 [signature]

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DECISION

This case involves a claim for refund or issuance of a tax credit certificate representing alleged erroneously paid final withholding tax for the month of October 2000 in the amount of FOUR HUNDRED FIVE THOUSAND THREE HUNDRED THIRTY ONE and 1/100 (P405,331.01) PESOS.

The antecedent facts of the case are as follows:

Petitioner is a domestic corporation duly organized and existing under and by virtue of Philippines laws, with principal office address at Suite 501, CTC Building, 2232 Roxas Boulevard, Pasay City, and is principally engaged in the business of power generation and subsequent sale thereof to its customers *(Summary of Admitted Facts, Paragraphs 1 and 3)*. It is registered with the Bureau of Internal

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Revenue (BIR) as a withholding agent with Taxpayer Identification Number (TIN) 002-234-275-000 *(Summary of Admitted Facts, Paragraph 4).*

Prior to petitioner's present name, it was originally registered as Hopewell Mobile Power Systems Corporation with the Securities and Exchange Commission (SEC), which was then changed to Southern Energy Mobile, Inc. Eventually, on March 6, 2001, petitioner again changed its name to Mirant (Philippines) Mobile Corporation, and was finally changed to its present name on July 18, 2001 *(Stipulation of the Facts, Paragraphs 1-3).*

For the month of June of 1998, petitioner availed of the services of Mitsubishi Corporation, a foreign corporation existing under the laws of Japan, whereby the latter rendered supervisory services relative to the maintenance of petitioner's Bulacan power plant *(Exhibits "H", "I", "J", "P", "Q" and "R"; TSN, August 14, 2003. p. 14).*

On November 10, 2000, petitioner, then under the corporate name Southern Energy Mobile, Inc., filed its Monthly remittance Return of Final Income Taxes Withheld for the month of October 2000 reflecting an amount of P405,331.30 as final taxes withheld from Mitsubishi Corporation *(Exhibit "A")*, detailed as follows:

Income Recipient	**Period Covered**	**Income Payment**	**Rate**	**FWT**
Mitsubishi	Oct-00	P 328,218.39	32%	P 105,029.89
Mitsubishi	Oct-00	382,598.64	32%	122,431.56
Mitsubishi	Oct-00	555,843.27	32%	177,869.85
		P 1,266,660.30		**P 405,331.30**

(Exhibit "A-3")

The final withholding tax for October 2000 was paid on November 10, 2000 as evidenced by Revenue Official Receipt No. 765456 reflecting a total amount of

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P405,331.30 in full payment of final and expanded withholding taxes due thereon *(Exhibit "B")*.

On January 31, 2001, petitioner filed its Annual Information Return of Income Taxes Withheld on Compensation and Final Withholding Taxes for the year 2000 reporting the details of final withholding taxes withheld from payments made to Mitsubishi Corporation on October 2000 *(Exhibit "C")*.

Subsequently, petitioner received two (2) letters from the Manila branch office of Mitsubishi Corporation requesting the refund of alleged excess withholding taxes withheld and remitted from the fees paid to Mitsubishi Corporation for supervisory services rendered on the ground that Mitsubishi Corporation should be classified as resident foreign corporation since it maintains a branch office in the Philippines. Hence, not subject to 32 % final withholding tax but only to 5% expanded withholding tax *(Exhibits "S" and "M")*. Thus, petitioner remitted the amount of JPY795,555.00 on January 24, 2002 to the Bank of Tokyo-Mitsubishi Ltd. Japan, Account No. 900030 as additional payment to Mitsubishi Corporation representing the excess amount deducted by petitioner from its income payments to Mitsubishi Corporation *(Exhibit "V"; TSN, January 28, 2004, pp. 21-24)*.

On July 12, 2002, petitioner filed an Amended Monthly Remittance Return of Creditable Income Taxes Withheld/Expanded and paid the five (5%) percent expanded withholding tax from its income payments to Mitsubishi Corporation *(Exhibits "F" and "G")*.

On November 7, 2002, within the reglementary period provided for by law, petitioner filed its administrative claim for refund with the BIR – RDO No. 51, Pasay City, in the amount of P405,331.01 representing the alleged erroneously withheld and remitted final withholding tax for the month of October 2000 *(Exhibit "L"; Stipulation of the Facts, Paragraph 4).*

Without waiting for any response from the respondent and in order to stop the running of the two-year prescriptive period, petitioner elevated the case through a Petition for Review with this Court on November 8, 2002 *(Stipulation of the Facts, Paragraph 8).*

By way of an Answer dated January 23, 2003, respondent asserted the following Special and Affirmative Defenses:

1. Petitioner's alleged claim for refund/tax credit is still subject to administrative routinary investigation/examination by the respondent's Bureau;

2. Taxes paid and collected are presumed to have been paid in accordance with law; hence, not refundable;

3. Petitioner failed to prove that the total amount of PHP405,331.01, representing the alleged erroneously paid final withholding tax for October, 2000 was fully substantiated;

4. BIR ruling No. 173-98 dated December 10, 1998 is not applicable to the issues involved in the instant case;

5. All income derived by Mitsubishi Corporation from all sources within the Philippines, being a non-resident foreign corporation, is subject to the final withholding taxes prescribed under par. I (1), Section 2.57.1 of Revenue Regulations No. 2-98, and not to the expanded/creditable withholding tax under Section 2.57.2 of the same Regulations;

6. Petitioner failed to prove that the alleged income tax payments from which final taxes were withheld were included in its gross income for calendar year 2000;

7. Assuming but without admitting the fact that petitioner is entitled to tax refund, it is incumbent upon the latter to show that it has complied with the provisions under Section 204 in relation to Section 230 (now 229) of the Tax Code. Otherwise, its failure to prove the same is fatal to its claim for refund;

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8. Claims for refund are construed strictly against the claimant for the same partakes 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)*.

The parties filed their Joint Stipulation of Facts and Issues on May 9, 2003 manifesting their mutual agreement on the issues involved in this case, to wit:

1. Whether or not the Petitioner has erroneously paid final withholding tax in the amount of PhP405,331.01 for October 2000;

2. Whether or not Mitsubishi Corporation is a non-resident foreign corporation; and

3. Whether all income derived by Mitsubishi Corporation from all sources within the Philippines is subject to expanded/creditable withholding tax of 5% pursuant to Section 2.57.2 of Revenue Regulations No. 2-98 or to final withholding tax of 32% pursuant to Section 2.57.1 of Revenue Regulations No. 2-98;

4. Whether or not the instant Petition for Review was filed within the two (2) year prescriptive period as provided in the NIRC;

5. Whether or not petitioner's claim for refund or issuance of tax credit certificate in the sum of P405,331.01 as erroneously paid final withholding tax for October 2000 is duly substantiated.

Petitioner rested its case after the presentation of its documentary and testimonial evidence while respondent merely submitted his case based on the pleadings *(Records, p. 252)*. The Court issued a resolution dated January 31, 2005 considering the case submitted for decision sans the memorandum of respondent.

After a cursory reading of the jointly stipulated facts and issues of the parties, this Court finds that the main issue in this case, despite the numerous matters raised, basically boils down to the basic question of whether or not petitioner is legally and factually entitled to a claim for refund or issuance of a tax credit certificate

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for its alleged erroneously paid final withholding tax in the amount of P405,331.01 for October 2000.

Petitioner anchored its claim for refund on Section 204(C), in relation to Section 229 of the Tax Code, to wit:

> "**SEC. 204. Authority of the Commissioner to Compromise, Abate and Refund or Credit Taxes.** -- The Commissioner may --
>
> xxx xxx xxx
>
> (C) Credit or refund taxes erroneously or illegally received or penalties imposed without authority, refund the value of internal revenue stamps when they are returned in good condition by the purchaser, and, in his discretion, redeem or change unused stamps that have been rendered unfit for use and refund their value upon proof of destruction. <u>No credit or refund of taxes or penalties shall be allowed unless the taxpayer files in writing with the Commissioner a claim for credit or refund within two (2) years after the payment of the tax or penalty</u>: x x x"
>
> "**SEC. 229. Recovery of Tax Erroneously or Illegally Collected.** -- No suit or proceeding shall be maintained in any court for the recovery of any national internal revenue tax hereafter alleged to have been erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority, or of any sum alleged to have been excessively or in any manner wrongfully collected, until a claim for refund or credit has been duly filed with the Commissioner; <u>but such suit or proceeding may be maintained</u>, whether or not such tax, penalty, or sum has been paid under protest or duress.
>
> <u>In any case, no such suit or proceeding 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</u>: x x x" *(Underscoring Ours)*

However, it is apropos to cite Section 58 of the 1997 Tax Code on returns and payments of taxes withheld at source in relation to the above provisions:

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> "**SEC. 58. Returns and Payment of Taxes Withheld at Source. –**
> **"(A) Quarterly Returns and Payments of Taxes Withheld. –** xxx
> xxx xxx xxx
>
> "The return for final withholding tax shall be filed and the payment made within twenty-five (25) days from the close of each calendar quarter, while the return for creditable withholding taxes shall be filed and the payment made not later than the last day of the month following the close of the quarter during which withholding was made: Provided, That the Commissioner, with the approval of the Secretary of Finance, may require these withholding agents to pay or deposit the taxes deducted or withheld at more frequent intervals when necessary to protect the interest of the government.

Revenue Regulations No. 2-98, in implementing Section 58 specifies the period for filing of monthly return and remittance of taxes withheld. To quote:

> "***Sec. 2.58. RETURNS AND PAYMENT OF TAXES WITHHELD AT SOURCE.***
> ***"(A) Monthly return and payment of taxes withheld at source –***
> ***"(1) WHERE TO FILE-***
> ***xxx xxx xxx***
> ***"(2) WHEN TO FILE-***
> "(a) The withholding tax return, whether creditable or final, shall be filed and payments should be made <u>within ten (10) days after the end of each month</u> except for taxes withheld for December which shall be filed on or before January 25 of the following year."

Applying the aforequoted provisions and considering further that respondent has already admitted the same, this Court finds that petitioner has indeed established the facts that it was able to file both its administrative and judicial claims for refund within the period required by law.

Based on the records, petitioner, under its former name Southern Energy Mobile, Inc., filed its Monthly Remittance Return of Final Income Taxes Withheld for

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the month of October 2000 on November 10, 2000 *(Exhibit "A")*. On the same date, petitioner likewise paid the amount of its total tax liability as stated in its return per Official Receipt No. 765456 *(Exhibit "B")*. Clearly, counting from the aforesaid date, petitioner has in fact until November 10, 2002 within which to file a claim for refund corresponding to its alleged erroneously paid tax. Hence, petitioner's administrative claim for refund filed on November 7, 2002 *(Exhibit "L")* and the Petition for Review filed before this Court on November 8, 2002 fall within the two-year prescriptive period. This resolves the fourth stipulated issue in the case under consideration.

Considering that the remaining issues are interrelated and intertwined, We shall resolve them jointly.

Petitioner contends that its payment of the amount of P405,331.01 representing the final withholding tax of 32% on its income payments to Mitsubishi Corporation was due to its erroneous belief that the latter is considered a nonresident foreign corporation. Citing BIR Ruling Nos. 173-98 (December 10, 1998) and 016-98 (February 6, 1998), petitioner argues that Mitsubishi Corporation should be considered, for tax purposes, as a resident foreign corporation for the reason that it maintains a branch office in the Philippines. Thus, its income payments made to the latter should not be subjected to the final withholding tax of 32% but instead to the 5% expanded/creditable withholding tax under Section 2.57.2 of Revenue Regulations No. 2-98.

Moreover, petitioner asserts that pursuant to the RP-Japan Tax Treaty, the income payments it made to Mitsubishi Corporation should be subject to 5% expanded withholding tax only and not to 32% final withholding tax. The pertinent provisions of the said treaty are hereunder quoted for easy reference:

"ARTICLE 7

(1) The profits of an enterprise of a Contracting State shall be taxable only in that Contracting State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in that other Contracting State but only so much of them as is attributable to that permanent establishment." *(Underscoring Ours)*

"ARTICLE 5

(1) For the purposes of this Convention, the term 'permanent establishment' means a fixed place of business through which the business of an enterprise is wholly or partly carried on.

(2) The term 'permanent establishment' includes especially:

(a) a store or other sales outlet;
(b) a branch;
(c) an office;
(d) a factory;
(e) a workshop;
(f) a warehouse;
(g) a mine, an oil or gas well, a quarry or other place of extraction of natural resources. x x x"

In applying the foregoing provisions, petitioner rationalizes that Mitsubishi Corporation, with head office in Japan and maintaining a branch office in the Philippines, resulted in its categorization as having set up a "permanent establishment" as contemplated by the above-quoted provisions of the RP-Japan Tax Treaty, in conjunction with the local tax laws. Petitioner believes that the income of Mitsubishi Corporation can be taxable in the Philippines only if it has done or carried business in the Philippines through a permanent establishment and the income could be attributable to that Philippine permanent establishment. Therefore, petitioner submits that the income derived by Mitsubishi Corporation from the

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supervisory services it rendered to the former were attributable to the latter's branch office in the Philippines, subjecting said income only to the 5% expanded/creditable withholding tax and not to the 32% final withholding tax it paid earlier.

To further bolster its claim, petitioner presented various invoices *(Exhibits "P, Q and R")*, purchase orders *(Exhibits "H, I and J")*, proofs of payment of said invoices *(Exhibits "H-3, I-3 and J-3")* and even Mitsubishi Corporation's license to do business in the Philippines *(Exhibit "N")*. Accordingly, it posits that the aforesaid foreign corporation is rightfully classified as "resident foreign corporation" subject to the 5% expanded withholding tax under Section 2.57.2 of Revenue Regulations No. 2-98.

To completely resolve the matter, this Court finds it important to first discuss the focal provisions of the 1997 NIRC in defining what constitutes a resident or non-resident foreign corporation, to wit:

> "**SEC. 22. Definitions.** – When used in this Title –
>
> xxx xxx xxx
>
> (H) The term *"resident foreign corporation"* applies to a foreign corporation <u>engaged in trade or business within the Philippines</u>.
>
> (I) The term *"nonresident foreign corporation"* applies to a foreign corporation <u>not engaged in trade or business within the Philippines</u>. x x x"*(Underscoring ours)*

Under Section 123 of the Corporation Code of the Philippines, "a foreign corporation is done, formed, organized or existing under any laws other than those of the Philippines and whose laws allow Filipino citizens and corporations to do business in its own country or State. It shall have the right to transact business in the Philippines after it shall have obtained a license to transact business in this country in accordance with this Code and a certificate of authority from the appropriate government agency". And for taxation purposes, a foreign corporation may be either a resident or nonresident, the former referring to a foreign corporation engaged in trade or business within the Philippines, and the latter, to a foreign corporation not engaged in trade or business in the Philippines and not having any office or place of business therein. *(De Leon, The Corporation Code of the Philippines Annotated, 2002 Ed., page 24)*

Given the facts of this case, petitioner substantially established that Mitsubishi Corporation, a corporation duly organized and existing by virtue of Japan laws, is indeed a "resident foreign corporation" as defined in this jurisdiction and consistent with the RP-Japan Tax Treaty. Petitioner presented as part of its evidence Mitsubishi Corporation's "Certificate of Filing of Amended Articles of Incorporation of a Foreign Corporation *(Exhibit "K")*", its "Application of Foreign Corporation to do Business in the Philippines Under the Provisions of Act No. 1459, As Amended *(Exhibit "N")*" and its "Certificate of Filing of Certificate of Amendment to the Articles of Incorporation on Change of Name of a Foreign Corporation *(Exhibit "O")*". Likewise, a careful scrutiny of the records reveals that Mitsubishi Corporation has been transacting business with petitioner through a branch office located at the 14th Floor, L. V. Locsin Bldg., 6752 Ayala Avenue, Makati City, Philippines *(Exhibits "M, S and T")*.

In addition, the fact that Mitsubishi Corporation is a resident foreign corporation has already been recognized by the respondent in BIR Ruling No. 173-98 (December 10, 1998), *viz*:

> "In reply, please be informed that since Mitsubishi Corporation has a branch office in the Philippines, it is considered to have a permanent establishment in the

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> Philippines. Therefore, Mitsubishi Corporation is a resident foreign corporation. One of the objects of operation of Mitsubishi Corporation – Philippine Branch per its Amended Articles of Incorporation is "agency, brokerage and wholesale..." with respect to its business in the Philippines xxx
>
> "xxx xxx xxx
>
> "Accordingly, pursuant to Section 2.57.2(B) of Revenue Regulations No. 2-98, this Office is of the opinion as it hereby holds that the commission to be paid to Mitsubishi Corporation in Japan is subject to the expanded withholding tax of 5% applicable to technical and management consultants."

Verily, the Supreme Court, in the case of ***The Mentholatum Co., Inc., et al. vs. Mangiliman et al., 72 Phil. 524***, discussed at length the true test in determining whether a foreign corporation is "doing or transacting business" in the Philippines to wit:

> " xxx The true test, however, seems to be whether the foreign corporation is continuing the body or substance of the business or enterprise for which it was organized or whether it has substantially retired from it and turned it over to another (Traction Cos. Vs. Collectors of Int. Revenue [C.C.A., Ohio], 223 F. 984, 987). The term implies a continuity of commercial dealings and arrangements, and contemplates, to that extent, the performance of acts or works or the exercise of some of the functions normally incident to, and in progressive prosecution of, the purpose and object of its organization."

Undoubtedly, before a foreign corporation may be regarded as doing business here in the Philippines, it is essential to prove that there is the intention on the part of the foreign corporation to establish a continuous business here in the Philippines. In other words, there must be a continuity, not only of the commercial dealings previously presented, but also, to an extent, the continuity of the performance of the acts or services typical, or incident to the purposes and objectives of the corporation.

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In the case at bar, considering that petitioner presented documentary evidences *(Exhibits "K, N and O")* showing that Mitsubishi Corporation has the intention of engaging/doing business in the Philippines as early as 1967, and continuously engaging/doing business up to the present through its branch office, the former has sufficiently met the quantum of proof that the latter has organized or created an office or place of business, or otherwise put up an agency to conduct its trade or business here in the Philippines, so as to be rightfully classified as resident foreign corporation. Clearly, the evidence adduced by the petitioner met the requirements under Article 5(2)(b) of the RP-Japan Tax Treaty in defining who are considered as having a "permanent establishment" in the Philippines.

In view of the foregoing premises, Mitsubishi Corporation is considered a resident foreign corporation within the contemplation of Philippine laws. Accordingly, Mitsubishi Corporation is not subject to the final withholding tax as provided for either under Section 28(B) of the 1997 NIRC, or under Section 2.57.1 of Revenue Regulations No. 2-98, but instead, it is subject to the expanded/creditable withholding tax under Section 2.57.2 of Revenue Regulations No. 2-98, which specifically provides:

> "***Sec. 2.57.2. Income payment subject to creditable withholding tax and rates prescribed thereon*** – 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:
>
> **(A) Professional fees, talent fees, etc., for services rendered by individuals** – On the gross professional, promotional and talent fees or any other form of remuneration for the services of the following individuals x x x:
>
> xxx xxx xxx

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(6) Management and technical consultants;

xxx xxx xxx

(B) Professional fees, talent fees, etc., for services of taxable juridical persons – On the gross professional, promotional and talent fees or any other form of remuneration enumerated in the preceding subparagraph for the services of taxable juridical persons – Five percent (5%)" *(Underscoring Ours)*

Indubitably, the income derived by Mitsubishi Corporation arising from the supervisory services it rendered to the petitioner is subject to the 5% expanded withholding tax and not to the 32% final withholding tax.

In fine, when petitioner filed an Amended Monthly Remittance Return of Creditable Income Taxes Withheld *(Exhibit "F")* and paid the amount of P84,584.70 representing the appropriate 5% expanded/creditable withholding tax from its income payments to Mitsubishi Corporation on July 12, 2002 per Official Receipt No. 1934305 *(Exhibit "G")*, the erroneous payment previously made by petitioner on November 10, 2000 in the amount of P405,331.30 as evidenced by Official Receipt No. 765456 *(Exhibit "B")* becomes refundable.

WHEREFORE, the instant petition is **GRANTED**. Accordingly, respondent is hereby **ORDERED** to **REFUND** or **ISSUE A TAX CREDIT CERTIFICATE** in the amount of P405,331.01 in favor of the petitioner for the erroneously paid final withholding tax for the month of October 2000.

SO ORDERED.

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Acting Presiding Justice

WE CONCUR:

ERLINDA P. UY
Associate Justice

OLGA PALANCA-ENRIQUEZ
Associate Justice

CERTIFICATION

I hereby certify that this Decision was reached after due consultation among the members of this Division in accordance with the provisions of Section 13, Article VIII of the Constitution.

JUANITO C. CASTAÑEDA, JR.
Chairman-2nd Division, and Acting Presiding Justice