REPUBLIC OF THE PHILIPPINES
Court Of Tax Appeals
QUEZON CITY

SECOND DIVISION

BANK OF THE PHILIPPINE ISLANDS,
Petitioner,

-versus-

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

C.T.A. CASE NO. 7484

Members:

CASTAÑEDA, JR., Chairperson
UY, and
PALANCA-ENRIQUEZ, JJ.

Promulgated:

JUN 25 2007

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DECISION

PALANCA-ENRIQUEZ, J.:

Are petitioner's Foreign Currency Deposit Unit (hereafter "FCDU") transactions, save for the 10% final tax, exempt from value added tax, documentary stamp tax and all other kinds of taxes?

THE CASE

This issue is before Us in this Petition For Review filed by the Bank of the Philippine Islands (hereafter "petitioner"), which seeks the reversal of the Final Decision on Disputed Assessment dated February

27, 2006 rendered by the OIC Assistant Commissioner of the Large Taxpayers Service of the Bureau of Internal Revenue in the Matter of the Protest of Bank of the Philippine Island against Assessment Notice No. LTS-LN # FCDU-116 DS-98-00013-05-000112, which found petitioner liable for deficiency documentary stamp tax (hereafter "DST"), pertinent portion of which reads as follows:

> "The records of this case disclosed that you have not introduced any evidence to overthrow the validity of our said findings.
>
> It is requested that your aforesaid deficiency documentary stamp tax liability be paid immediately upon receipt hereof, inclusive of penalties incidents to delinquency. This is our final decision. If you disagree, you may appeal this final decision with the Court of Tax Appeals within thirty (30) days from date of receipt hereof, otherwise our said deficiency income tax assessment shall become final, executory and demandable."

THE FACTS

The facts of the case, as culled from the records, are as follows:

Petitioner Bank of the Philippine Islands is a banking corporation, organized and existing under and by virtue of the laws of the Republic of the Philippines, with principal office at the Bank of the Philippine Islands Building, Ayala Avenue, Makati City. Petitioner, allegedly (as surviving

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corporation) merged with Prudential Bank (as absorbed corporation) on December 29, 2005 whereby the entire assets and liabilities of Prudential Bank were transferred and absorbed by petitioner. As a banking institution, it has FCDU engaged in foreign currency transactions.

Respondent Bureau of Internal Revenue, through the Commissioner of Internal Revenue (hereafter "respondent"), is the agency of the government tasked with the enforcement of revenue laws and collection of taxes and duties.

On October 13, 2004, petitioner received from the respondent a Preliminary Assessment Notice dated September 17, 2004 (hereafter "PAN"), demanding payment of alleged deficiency DST on petitioner's Foreign Currency Deposit Unit (hereafter "FCDU") transactions in the amount of P21,672,955.83, inclusive of interest, surcharge and compromise penalty covering taxable year 1998.

On October 26, 2004, petitioner filed a letter dated October 25, 2004, requesting for the cancellation of the aforesaid PAN for lack of legal and factual bases.

On March 4, 2005, respondent issued a Formal Letter of Demand/Assessment Notice demanding payment of petitioner's alleged deficiency DST on its FCDU transactions for taxable year 1998 in the amount of P22,426,146.42.

On March 18, 2005, petitioner administratively protested said Formal Letter of Demand alleging, among others, that its onshore income on FCDU transactions are, save for the ten percent (10%) final tax, exempt from all taxes such as DST. Moreover, petitioner contended that the assessment is already barred by prescription for having been issued beyond the three (3) year period provided under Section 203, in relation to Section 200 of the National Internal Revenue Code (hereafter "NIRC"), and the assessment has no factual basis.

On April 4, 2006, petitioner received the Final Decision dated February 27, 2006 of respondent demanding payment of petitioner's alleged deficiency DST on FCDU transactions in the amount of P24,366,490.51 for year 1998, computed as follows:

DOCUMENTARY STAMP TAX-FCDU	
Loans	P2,041,609,451.00
Deposit liabilities	3,903,551,046.00
Bills payable	40,452,168.00
Total	5,985,612,665.00
DST Rate	.30/200
DST due thereon	8,978,419.00
Add: 25% surcharge	2,244,604.75

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20% interest from 1-10-1999 to 4-30-2006[146.1111%]	13,118,466.76
Compromise penalty	25,000.00
TOTAL TAX & PENALTIES	P24,366,490.51

On May 4, 2006, petitioner filed the instant Petition for Review.

In his "Answer" filed on July 17, 2006, respondent denied the material allegations of the petition.

Issues having been joined, the case was set for pre-trial.

At the pre-trial held on August 31, 2006, both parties stipulated that the issues involved in the instant case are purely legal and agreed to dispense with trial and moved that they just be allowed to file their respective memoranda in support of their respective positions, which the Court granted.

On March 26, 2007, petitioner filed its "Memorandum", while respondent failed to file the same despite notice. Hence, the case was deemed submitted for decision.

ISSUES

The petitioner raised the following issues for this Court's consideration:

I

WHETHER OR NOT PETITIONER'S FCDU TRANSACTIONS ARE, SAVE FOR THE 10% FINAL TAX, EXEMPT FROM VALUE ADDED TAX AND DOCUMENTARY STAMP TAX AND ALL OTHER KINDS OF TAXES.

II

WHETHER OR NOT THE AMOUNT INDICATED IN RESPONDENT'S FORMAL LETTER OF DEMAND/ASSESSMENT NOTICE IS ARBITRARY AND LACKS FACTUAL BASIS.

III

WHETHER OR NOT THE ASSESSMENT HAS ALREADY PRESCRIBED.

Principal Issue:

The foregoing issues raised by petitioner boil down to the principal issue of whether or not petitioner's FCDU transactions are, save for the 10% final tax, exempt from value added tax, documentary stamp tax and all other kinds of taxes.

Petitioner BPI's Theory

Invoking *Presidential Decree No. 1035*, Expanding the Authority of Depository Banks under Republic Act No. 6426, petitioner posits that offshore income derived by FCDUs is subject to a 5% tax in lieu of all

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taxes, while onshore income is subject to a 10% final withholding tax, similarly in lieu of all taxes; that *Revenue Regulations No. 10-76*, as amended by *Revenue Regulations No. 14-77,* provides that the tax imposed on both offshore and onshore income of FCDUs is in lieu of all taxes, such as, but not limited to privilege tax, gross receipt tax, documentary and science stamp tax and profit remittance tax; that similar to the other Tax Code, the 1997 Tax Code does not expressly repeal the provisions of *PD No. 1035* granting exemption to FCDUs from all taxes other than a final tax on certain income, neither does it impliedly repeal *PD No. 1035*; that repeal by implication is generally frowned upon for the intention to repeal must be clear and manifest. In brief, it is petitioner's theory that absent any express repeal by the *1997 Tax Code*, the provisions of the Foreign Currency Deposit Act subjecting FCDU transactions to 10% final tax and exempting the same from all other taxes remain effective.

Invoking *Republic Act No. 9294*, restoring the tax exemptions of OBUs and FCDUs, petitioner further argues that *Republic Act No. 9294* is a curative statute which should be applied retroactively, effective upon the enactment of the 1997 Tax Code and further cited the deliberations of

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the Committee on Ways and Means of the House of Representatives held on May 20, 2003.

Respondent Commissioner's Theory

Citing the case of *ING Bank (Manila Branch) vs. Commissioner of Internal Revenue, CTA Case No. 6017, dated March 11, 2002*, respondent, counter-argues that the phrase "exempt from all taxes" has been deleted by the legislators. The amendment by deletion of certain words or phrases in a statute indicates that the legislature intended to change the meaning of the statute *(Gloria vs. Court of Appeals, 306 SCRA 287)*. By virtue of such deletion, *Revenue Regulations No. 10-76*, which implemented the old law, is no longer applicable. In other words, the payment of the 10% final tax on FCDU income does not exempt petitioner from the payment of branch profit remittance tax or other taxes for that matter.

THE COURT'S RULING

The petition has no merit.

The Tax Reform Act of 1997, as Amended is the Applicable Statute to Petitioner, Not R.A. No. 9294

While We agree with the petitioner that *R.A. No. 9294*, otherwise known as *"An Act Restoring The Tax Exemption Of Offshore Banking Units (OBUs) And Foreign Currency Deposit Units (FCDUs), Amending For The Purpose Section 27 (D) And Section 28, Paragraphs (A) (4) And (A) (7) (B) Of The National Internal Revenue Code As Amended"* has restored the tax exemptions previously granted to FCDUs of depository banks by *P.D. No. 1035, as amended,* the same however, took effect only on May 21, 2004. Consequently, prior to the effectivity of *R.A. No. 9294*, or from January 1, 1998 to May 20, 2004, the *Tax Reform Act of 1997* is the governing law with respect to the taxability of FCDUs of depository banks on their foreign currency transactions.

Tracing back to the original law, *R.A. No. 6426*, otherwise known as the *"Foreign Currency Deposit Act of the Philippines"*, as amended by *P.D. No. 1035*, expanding the foreign currency lending authority of the depository banks, as further amended by *P.D. No. 1246*, all foreign currency deposits made under the foreign currency deposit system, including interest and all other income of such deposits were exempt from all taxes, irrespective of whether or not these deposits were made by residents or non-residents. Thus, *Section 6 of R.A. No. 6426*, as amended, provides:

> "SEC. 6. Tax Exemptions. – All foreign currency deposits made under this Act, as amended by Presidential Decree No. 1035, as well as foreign currency deposits authorized under Presidential Decree No. 1034, including interest and all other income or earnings of such deposits, are hereby exempted from any and all taxes whatsoever irrespective of whether or not these deposits are made by residents or non-residents so long as the deposits are eligible or allowed under aforementioned laws and in the case of non-residents, irrespective of whether or not they are engaged in trade or business in the Philippines."

However, upon the effectivity of the *Tax Reform Act of 1997* on January 01, 1998, the phrase "are hereby exempted from any and all taxes whatsoever" contained in *Section 6 of R.A. No. 6426*, as amended, was deleted. *Section 27 (D) (3)* of the *Tax Reform Act of 1997, as amended,* reads as follows:

> "SEC. 27. – *Rates of Income Tax on Domestic Corporations.* –
>
> xxx xxx
>
> (D) Rates of Tax on Certain Passive Income. –
>
> xxx xxx
>
> (3) *Tax on Income Derived under the Expanded Foreign Currency Deposit System.* — Income derived by a

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> depository bank under the expanded foreign currency deposit system from foreign currency transactions with local commercial banks, including branches of foreign banks that may be authorized by the Bangko Sentral ng Pilipinas (BSP) to transact business with foreign currency depository system units and other depository banks under the expanded foreign currency deposit system, including interest income from foreign currency loans granted by such depository banks under said expanded foreign currency deposit system to residents, shall be subject to a final income tax at the rate of ten percent (10%) of such income.
>
> Any income of nonresidents, whether individuals or corporations, from transactions with depository banks under the expanded system shall be exempt from income tax."

Pursuant to the aforequoted provision, tax exemption privileges previously granted to FCDUs of depository banks on their foreign currency transactions were definitely deleted by the legislature. In the case of *Gloria vs. Court of Appeals, 306 SCRA 287,* the Supreme Court has categorically ruled that "as a rule, the amendment by deletion of certain words or phrases in a statute indicates that the legislature intended to change the meaning of the statute, for the presumption is that the legislature would not have made the deletion had the intention been not in effect a change in its meaning. The amended statute should accordingly be given a construction different from that previous to its amendment." By virtue of such deletion, *R.A. Act No. 6264, as amended*, and its

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implementing *Revenue Regulations No. 10-76*, are no longer applicable. In other words, the payment of the 10% final tax on FCDU income does not exempt petitioner from the payment of documentary stamp tax.

By express provision of *Section 27 (D) (3) of the Tax Reform Act of 1997, as amended*, the ten percent (10%) final tax levied on the income of FCDUs of depository banks pertain to income derived by depositary banks under the expanded foreign currency deposit system. It does not include DST, which is an excise tax *(Lincoln Philippines Life Insurance Co. vs. Court of Appeals, 293 SCRA 99)*. As such, DST is thus levied on the exercise of these privileges through the execution of specific instruments independently of the legal status of the transaction giving rise thereto *(Philippine Home Assurance Corp., et. al vs. Court of Appeals, 301 SCRA 447-448)*. In the case at bench, DST is imposed upon petitioner's exercise of the privilege of engaging in foreign currency transactions or business.

Furthermore, upon a careful examination and scrutiny of *R.A. No. 9294*, there is no provision in the said law, which grants petitioner exemption from payment of DST. Neither does the said law provide its application to assessment of deficiency taxes for FCDU transactions transpiring before its effectivity. Clearly, petitioner is liable for the payment of its deficiency DST for year 1998.

Basic is the rule that laws shall have no retroactive effect, unless the contrary is provided *(Article 4 of the New Civil Code)*. It is a fundamental principle that the validity and obligatory force of a law proceed from the fact that it has first been promulgated. A law that is not yet effective cannot be considered as conclusively known by the populace. To make a law binding even before it takes effect may lead to the arbitrary exercise of the legislative power. *Nova constitutio futuris formam imponere debet non praeteritis.* A new state of the law ought to affect the future, not the past. Any doubt must generally be resolved against the retroactive operation of laws, whether these are original enactments, amendments or repeals *(Mighty Corporation, et. al. vs. E. & J. Gallo Winery, et. al., 434 SCRA 491).*

R.A. No. 9294 is Not a Curative Statute

Petitioner's contention that *R.A. No. 9294* is a curative statute, hence the same must be applied retroactively, cannot be sustained.

Curative statutes are enacted to cure defects in a prior law or to validate legal proceedings, which would otherwise be void for want of

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conformity with certain legal requirements. They are intended to supply defects, abridge superfluities and curb certain evils. They are intended to enable persons to carry into effect that which they have designed or intended, but has failed of expected legal consequence by reason of some statutory disability or irregularity in their own action. They make valid that which, before the enactment of the statute was invalid. Their purpose is to give validity to acts done that would have been invalid under existing laws, as if existing laws have been complied with *(Ramatek Philippines, Inc. vs. De los Reyes, 474 SCRA 140-141)*. Simply stated, curative statutes are intended to make valid that which before enactment of the statute was invalid *(Tatad vs. Garcia, Jr., 243 SCRA 462)*.

Section 27, (D) (3) of the Tax Reform Act of 1997, as amended, is explicit and clear. It deleted the phrase, "are hereby exempted from any and all taxes whatsoever". It is an elementary rule in statutory construction that if a statute is clear, plain and free from ambiguity, it must be given its literal meaning and applied without attempted interpretation. *Verba legis non est recedendum*. From the words of a statute there should be no departure *(Del Mar vs. Philippine Amusement and Gaming Corp., 358 SCRA 781)*.

Applying the aforementioned jurisprudence to the instant case, it is evident that *R.A. No. 9294* is not a curative statute. Consequently, the same cannot be applied retroactively. Petitioner cannot, therefore, find solace in *R.A. No. 9294*, restoring the tax exemption privileges originally granted to FCDUs by *PD. No. 1035, as amended.*

Second Issue

Anent the second issue, claiming that the amount indicated in the formal letter of demand/assessment notice is arbitrary and lacks factual basis, petitioner invokes *Section 228 of the Tax Code*, which states that the taxpayer shall be informed of the law and the facts on which the assessment is made, otherwise, the assessment shall be null and void.

Respondent, on the other hand, counter-argues that the amount indicated in the formal letter of demand/assessment notice and final decision on disputed assessment is not arbitrary and does not lack factual basis. It posits that the assessment for deficiency DST on FCDU was based on the amount of loans, time deposits and bills payable amounting to P2,041,609,451.00, P3,903,551,046.00 and P40,452,168.00 respectively, which were stated in petitioner's FCDU Income Tax

Returns and Audited Financial Statements filed with the Bureau of Internal Revenue.

The Formal Letter of Demand and Assessment Notice have Factual and Legal Bases

Petitioner's contentions are bereft of merit.

Section 228 of the Tax Reform Act of 1997, as amended, provides:

> "SEC. 228. Protesting of Assessment. – When the Commissioner or his duly authorized finds that proper taxes should be assessed, he shall first notify the taxpayer of his findings: Provided, however, That a preassessment notice shall not be required in the following cases:
>
> xxx xxx
>
> The taxpayer shall be informed in writing of the law and the facts on which the assessment is made; otherwise the assessment shall be void.
>
> xxx xxx."

Pursuant to aforecited provision, the taxpayer shall be informed in writing of the law and the facts on which the assessment is made. The assessment notices need not be a full narration of the facts and laws on which the assessment is based. So long as the parties are notified and were given the opportunity to explain their side, the requirements of due process are satisfactorily complied with (*Calma vs. Court of Appeals, 302 SCRA 689*).

Upon a careful review of the evidence on record, the Court holds that petitioner was properly notified of the assessment of its tax liability and was given the opportunity to explain its side. On October 13, 2004, petitioner received from respondent a Preliminary Assessment Notice dated September 17, 2004 *(Annex "A", Petition for Review)*, wherein petitioner was informed of its deficiency DST liability with the corresponding surcharge, interest and penalty on the basis of *Sections 180, 248 (A) and 249 (B),* respectively, of the *Tax Reform Act of 1997, as amended.* Attached to the said PAN is the Details of Discrepancy, which shows the breakdown of the basic deficiency DST. The composition of the accounts subject to basic deficiency DST was taken from petitioner's Annual Income Tax Return-FCDU for the year ended 1998, filed with the Bureau of Internal Revenue on April 15, 1999. On account of the said PAN, petitioner, in a Letter dated October 25, 2004 *(Annex "B", Petition for Review)*, protested the said assessment.

Likewise, on March 11, 2005, petitioner received from respondent a Formal Letter of Demand *(Annex "C", Petition for Review)*, containing the

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same information found in the PAN, but with the adjusted interest liability and demand for payment of the deficiency tax liability. Attached to the said PAN are the Details of Discrepancy and the Audit Result/Assessment Notice. By reason of said Formal Letter of Demand and Assessment Notice, petitioner was able to prepare a comprehensive Protest Letter/Request for Reconsideration *(Annex "D", Petition for Review)*, propounding the very same issues raised in the instant Petition. Had petitioner not been sufficiently informed of the facts and the laws on which the assessment was based, it could not have protested in full. From the foregoing, the inescapable conclusion therefore, is that the Formal Letter of Demand has factual and legal bases.

Third Issue

As regards the third issue, invoking that the respondent's assessment for alleged deficiency DST for year 1998 had already prescribed, petitioner contends that pursuant to *Section 203 of the Tax Reform Act of 1997*, internal revenue taxes shall be assessed within three (3) years after the last day prescribed by law for the filing of the return, and no proceeding in court without assessment for the collection of such taxes shall be begun after expiration of such period; that for taxable year

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1998, the assessment for the alleged deficiency DST should have been issued not later than the 5th day of January 2002 considering that the filing/payment of DST for the last month of year 1998 is considered to have been filed on the 5th day of January 1999.

Refuting petitioner's allegation that the assessment has already prescribed, respondent counters that the assessments were issued within the reglementary period of ten (10) years considering that this is a case of failure to file a return under *Section 222 of the Tax Reform Act of 1997, as amended.*

The Assessment has Not Yet Prescribed

We agree with the respondent.

Section 222 of the Tax Reform Act of 1997, as amended, provides that in case failure to file a return, the tax may be assessed within ten (10) years from the discovery of the omission, to wit:

> "SEC. 222. – Exceptions as to Period of Limitation of Assessment and Collection of Taxes. –
>
> (a) In the case of a false or fraudulent return with intent to evade tax or of failure to file a return, the tax may be assessed, or a proceeding in court for the collection of such tax may be filed without assessment, at any time within ten (10) years after the discovery of the falsity, fraud

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or omission: Provided, That in a fraud assessment which has become final and executory, the fact of fraud shall be judicially taken cognizance of in the civil or criminal action for the collection thereof.

xxx xxx."

In this regard, *Section 200 of the Tax Reform Act of 1997, as amended,* provides the time for filing and payment of the DST, as follows:

"SEC. 200. Payment of Documentary Stamp Tax. –

xxx xxx

(B) Time for Filing and Payment of the Tax. – Except as provided by rules and regulations promulgated by the Secretary of Finance, upon recommendation of the Commissioner, the tax return prescribed in this Section shall be filed within ten (10) days after the close of the months when the taxable document was made, signed, issued, accepted or transferred, and the tax thereon shall be paid at the same time the aforesaid return is filed.

xxx xxx."

Pursuant to the aforementioned provision, petitioner is obliged to file its DST tax return and pay within ten (10) days after the close of the month when the taxable document was made, signed, issued, accepted or transferred. However, as admitted by the petitioner itself in its Protest

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Letter dated March 15, 2005 and in its Petition for Review, it did not file any DST return on its FCDU. Being a clear case of omission to file a return, the applicable prescriptive period is ten (10) years from the discovery of the said omission.

Record shows that petitioner filed its Annual Income Tax Return on its FCDU for taxable year 1998 on April 15, 1999, while the Formal Letter of Demand and Final Assessment Notice was issued on March 4, 2005. Clearly, the assessment was issued within the ten (10) year prescriptive period.

For all the foregoing, the Court finds the Final Decision on Disputed Assessment of the OIC Assistant Commissioner of the Large Taxpayers Service of the Bureau of Internal Revenue is not flawed by reversible error, but on the contrary, conforms to the evidence on record and the applicable laws and jurisprudence. We, therefore, affirm the same.

However, considering that there was no compromise agreement between the parties, the compromise penalty of P25,000.00 imposed by respondent is hereby deleted. Hence, the total amount due is only P24,341,490.51.

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Finally, petitioner is liable to pay 20% delinquency interest on the total amount due of P24,341,490.51, computed from April 04, 2006 until full payment thereof, pursuant to *Section 249 (C) of the Tax Reform Act of 1997, as amended.*

WHEREFORE, premises considered, the Petition For Review is hereby **DISMISSED** for lack of merit. With the above modifications, the Final Decision on Disputed Assessment dated February 27, 2006 of the OIC Assistant Commissioner of the Large Taxpayers Services of the Bureau of Internal Revenue is hereby **AFFIRMED** in all other respects. Accordingly, petitioner is ordered to pay the respondent the total amount of Twenty Four Million Three Hundred Forty One Thousand Four Hundred Ninety and 51/100 Pesos (P24,341,490.51), representing the total deficiency DST, surcharge and delinquency interest, plus twenty percent (20%) delinquency interest thereon computed from April 04, 2006 until full payment thereof, pursuant to *Section 249 (C) of the Tax Reform Act of 1997, as amended.*

SO ORDERED.

OLGA PALANCA-ENRIQUEZ
Associate Justice

WE CONCUR:

JUANITO C. CASTAÑEDA, JR.
Associate Justice

ERLINDA P. UY
Associate Justice

ATTESTATION

I attest that the conclusions in the above Decision were reached in consultation before the cases were assigned to the writer of the opinion of the Court's Division.

JUANITO C. CASTAÑEDA, JR.
Associate Justice
Chairman, Second Division

CERTIFICATION

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

ERNESTO D. ACOSTA
Presiding Justice