REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

EN BANC

THE SECRETARY OF FINANCE,
Petitioner,

-versus-

COURT OF TAX APPEALS, THIRD DIVISION, EGIS ROAD OPERATIONS, S.A.,
Respondents.

CTA EB NO. 1668
(CTA Case No. 8414)

Present:

Del Rosario, *P.J.*,
Castañeda, Jr.,
Uy,
Fabon-Victorino,
Mindaro-Grulla,
Ringpis-Liban, *and*
Manahan, *JJ.*

Promulgated:

NOV 20 2018
4:23 p.m.

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DECISION

CASTAÑEDA, JR., J.:

Before the Court *En Banc* is a Petition for Review filed by The Secretary of Finance under Rule 8 Section 3 of the Revised Rules of the Court of Tax Appeals (RRCTA) in relation to Rule 43 of the Rules of Court seeking to annul and set aside of the following:

1. December 15, 2016 Decision[1] of the CTA Third Division[2] the dispositive portion of which reads:

> "**WHEREFORE**, premises considered, the Petition for Review is **GRANTED**. Accordingly, the ruling of the Secretary of Finance dated November 15, 2011 and BIR Ruling No. ITAD 210-11 dated August 15, 2011 are **REVERSED** and **SET ASIDE**.
>
> **SO ORDERED**."

[1] Annex A, Petition for Review, Rollo, pp. 46-66.
[2] Penned by J. Ma. Belen M. Ringpis-Liban with the concurrence of J. Esperanza R. Fabon-Victorino. J. Lovell R. Bautista was on leave.

2. May 23, 2017 Resolution[3] denying both the Motions for Reconsideration of herein petitioner and respondent for lack of merit.

THE FACTS

The facts, quoted from the December 15, 2016 Decision and condensed from the records, are as follows:

Respondent EGIS Road Operation S.A. (ERO S.A.) is a nonresident foreign corporation organized and existing under the laws of France with principal address at 11 Avenue du Center, 78 280 Guyancourt, France and with Philippine Tax Identification Number 293-638-147-000. ERO S.A. is not registered as a corporation or partnership licensed to do business in the Philippines and does not conduct business in the Philippines.[4]

In BIR Ruling No. DA-ITAD 037-09 dated March 18, 2009, the Commissioner of Internal Revenue (CIR) confirmed the 10% preferential tax rate on the payment of dividends received by ERO S.A. from Tollways Management Corporation pursuant to the Convention between the Government of the Republic of the Philippines and the Government of the French Republic for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income (RP-France Tax Treaty).[5]

On April 20, 2010, the Board of Directors of Egis Road Operations Philippines, Inc. (ERO Philippines), a corporation organized and existing under the laws of the Philippines, approved the declaration of cash dividend of ₱60,000,000 in favor of its stockholders of record as of December 31, 2009 and payable within the year 2010. The Corporate Secretary of ERO Philippines certified that as of April 20, 2010, ERO S.A. is the stockholder of 79,595 common shares of stock of ERO Philippines, with a par value of ₱100.00 per share, or a total par value of ₱7,959,500.00, equivalent to 99% of the total issued and outstanding shares of ERO Philippines.[6]

On May 6, 2010, ERO Philippines paid dividends to ERO S.A.[7]

On August 25, 2010, the CIR issued Revenue Memorandum Order (RMO) No. 72-2010 entitled, "Guidelines on the Processing of Tax Treaty Relief Applications (TTRA) Pursuant to Existing Philippine Tax Treaties" and addressed to all revenue officials and personnel and others concerned. The RMO took effect on November 4, 2010.[8]

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[3] Annex B, Petition for Review, Rollo, pp. 67-69.
[4] Decision, Rollo, pp. 47-48.
[5] Decision, Rollo, p. 48.
[6] *Id.*
[7] *Id.*
[8] *Id.*

On August 31, 2010, ERO Philippines again paid dividends to ERO S.A.[9]

On March 18, 2011, ERO S.A. filed a Tax Treaty Relief Application (TTRA) dated March 17, 2011 with the International Tax Affairs Division (ITAD) of the Bureau of Internal Revenue (BIR) to request confirmation that the dividends paid by ERO Philippines to ERO S.A. on May 6, 2010 and on August 31, 2010 are subject to the preferential tax rate of 10% pursuant to the RP-France Tax Treaty, as amended by the Protocol to the Tax Convention between the Government of the Republic of the Philippines and the Government of the French Republic effective January 1, 1998.[10]

On August 15, 2011, the former BIR Commissioner Kim S. Jacinto Henares issued BIR Ruling No. ITAD 210-11 denying ERO S.A.'s TTRA on the ground that it was disqualified from the tax treaty relief sought as the application was not filed within the period provided under RMO No. 72-2010. Consequently, instead of a reduced rate of ten percent (10%), the dividends paid to ERO S.A. would be subject to income tax at the regular rate of thirty percent (30%) of the gross amount thereof, under Section 28(B)(1) of the 1997 NIRC, as amended, thus:

> "In reply, please be informed that Section 14 and 13 of Revenue Memorandum Order ('RMO') No. 72-2010 which was published in the Manila Bulletin on October 20, 2010, and effective November 4, 2010, provides that:
>
> *'Section 14. WHEN AND WHERE TO FILE THE TTRA.-*
>
> *XXX XXX XXX*
>
> *Filing should always be made BEFORE the transaction. Transaction for purposes of filing the TTRA shall mean before the occurrence of the first taxable event. Failure to properly file the TTRA with ITAD within the period prescribed herein shall have the effect of disqualifying the TTRA under the* RMO.
>
> *Section 13. DEFINITIONS.-*
>
> *XXX XXX XXX*
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> 4. First taxable event *for purposes of filing the Tax Treaty Relief Application (TTRA), shall mean the first or the only time when the income payor is required to withhold the income tax thereon or should have withheld taxes thereon had the transaction been subjected to tax ...*

[9] *Id.*
[10] Decision, Rollo, pp. 48-49.

Under RMO 72-2010, the filing of TTRAs should be made **before** the occurrence of the **first taxable event**, or the first or the only time when an income payor is required to withhold income tax on payments subject to preferential treatment. The **first and only time** referred herein corresponds to the **period a withholding agent is required to file the necessary returns on final and creditable income taxes withheld in a particular month, which is within ten days after the end of that month**, or, if the withholding was made in **December, on or before January 15 of the following year**, pursuant to Section 2.58(A)(2) of **Revenue Regulations No. 2-98 (Implementing Republic Act No. 8424, 'An Act Amending the National Internal Revenue Code, as amended' Relative to the Withholding on Income Subject to the Expanded Withholding Tax and Final Withholding Tax, Withholding of Income Tax on Compensation, Withholding of Creditable Value-Added Tax and Other Percentage Taxes)**, thus:

> *'Section 2.58. RETURNS AND PAYMENT* OF *TAXES WITHHELD AT SOURCE.-*
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> (A) Monthly return and payment of taxes withheld at source-
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> *XXX XXX XXX*
>
> (2) WHEN TO FILE. -
>
> *(a) For both large and non-large taxpayers, the withholding tax return, whether creditable or final (including final withholding taxes on interest from any currency bank deposit and yield or any other monetary benefit from deposit substitutes and from trust funds and similar arrangements) shall be filed and payments should be made within ten (10) days after the end of each month, except for taxes withheld for the month of **December of each year**, which shall be filed on or before **January 15 of the following year** ... ' (Emphasis added)*

Accordingly, since the TTRA in question was filed on **March 18, 2011**, the first taxable event that corresponds to that date falls on or before **April 10, 2011**, as if **ERO Philippines** made a payment in March 2011 and would then file a monthly income tax return thereon until April 10, 2011. With respect to dividends paid by **ERO Philippines** to **ERO S.A.** on any date in the year 2010, or at the latest, **December 31, 2010**, the filing of the corresponding TIRA should have been made **before January 15, 2011**, pursuant to RMO 72-2010. However, since the TTRA for such dividends paid by **ERO Philippines** to **ERO S.A.** was **not** filed within the prescribed period of filing, such dividends are therefore **disqualified** from the relief being sought for. This being the case, instead of a reduced rate of 10 percent, the dividends paid to **ERO S.A.** are subject to income tax at the regular rate of 30 percent of the gross amount thereof, under Section 28(B)(1)(a) [sic] of the National Internal Revenue Code of 1997, as amended, thus:

> *'Section 28. Rates if Income Tax on Foreign Corporations. -*
>
> *XXX XXX XXX*

> *(B) Tax on Nonresident Foreign Corporation. -*
>
> (1) ***In General***- *Except as otherwise provided in this Code, a foreign Corporation not engaged in trade or business in the Philippines shall pay a tax equal to thirty-five percent (35%) of the gross income received during each taxable year from all sources within the Philippines, such as interests, dividends, rents, royalties, salaries, premiums (except reinsurance premiums), annuities, emoluments or other fixed or determinable annual, periodic or casual gains, profits and income, and capital gains, except capital gains subject to tax under subparagraph 5(c) and (d) above: Provided, That effective January 1, 2009, the rate of income tax shall be thirty percent (30%)'"*

On September 14, 2011, ERO S.A. appealed to the Department of Finance (DOF) Secretary for the review and reversal of BIR Ruling No. ITAD 210-11 alleging that the ruling is unlawful in view of its retroactive application of the provisions of RMO No. 72-2010 and that the CIR exceeded the granted authority to implement tax treaties by providing, under the terms of the RMO, additional requirements not otherwise stated in the law or treaty that it seeks to implement.[11]

On November 15, 2011, the DOF Secretary affirmed the ruling of the CIR, thus:[12]

> "Based on the foregoing, we hereby **affirm** the ruling of the Commissioner in its entirety. The dividends paid by ERO Philippines to ERO [ERO S.A.] on **6 May and 31 August 2010** will be subject to regular income tax of 30% of the gross amount thereof, under Section 28(B)(1)(a) [sic] of NIRC, as amended."

CTA Proceedings

On January 24, 2012, petitioner filed a Petition for Review before the Court of Tax Appeals (CTA).[13]

The CIR filed an Answer on April 3, 2012, while Secretary of Finance filed an Answer on April 30, 2012 essentially raising the following Special and Affirmative Defenses:[14]

1. The petition is procedurally infirm; the subject matter of the present suit is within the jurisdiction of the Regional Trial Court, not the CTA; *gr*

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[11] Decision, Rollo, p. 52.
[12] Decision, Rollo, p. 54.
[13] *Id.*
[14] Decision, Rollo, pp. 54-55

2. Assuming for the sake of argument that the CTA has jurisdiction over the instant petition, the same should still be dismissed for failure of petitioner to comply with the procedural requirements for the availment of the preferential tax rate under the RP-France Tax Treaty;

3. RMO No. 72-2010 has prospective application;

4. The dividends paid to petitioner are not entitled to the 10% preferential tax rate; and

5. The rulings of the CIR and the Secretary of Finance have the force and effect of law.

The case was set for pre-trial conference on June 15, 2012. After filing their respective Pre-Trial Briefs on June 8, 2012, the parties entered into a Joint Stipulation of Facts and Issue. Thereafter, the pre-trial was terminated and trial on the merits ensued.[15]

Based on the Pre-Trial Order, the parties agreed to submit two issues, to wit:

1. Whether or not the Honorable Court of Tax Appeals has jurisdiction over the subject matter of the instant case; and,

2. Whether or not the Dividends paid by ERO Philippines to petitioner are subject to 10% Preferential Rate provided under the RP-France Double Tax Treaty.

During the initial presentation of petitioner's evidence, counsel for respondent Secretary of Finance moved for the early resolution of the issue on jurisdiction.

Subsequently, both the Secretary of Finance and the CIR filed their Motions to Dismiss assailing the Court's authority to hear and determine the petition. According to them, the subject matter of the case falls within the jurisdiction of the Regional Trial Courts and not within the CTA's special jurisdiction. The authority conferred upon the CTA under Section 7 of Republic Act (RA) No. 1125, as amended, does not include jurisdiction over cases where the constitutionality of a law or rule is challenged.[16]

Meanwhile, ERO S.A. opposed the dismissal of the case. In its Comment, ERO S.A. stated that the petition sought a review of the Decision or ruling of the Secretary of Finance dated November 15,2011 which affirmed BIR Ruling No. ITAD 210-11 dated August 15, 2011 and the constitutionality of the RMO was but one of the issues raised in the petition. According to ERO

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[15] Decision, Rollo, p. 55.
[16] *Id.*

S.A., the CTA may just ignore the constitutionality issue and resolve the other issues raised in the petition. Furthermore, the CTA has exclusive appellate jurisdiction to review by appeal the decisions of respondent CIR involving matters arising under the NIRC, as stated in Section 7(a)(1) of RA No. 1125, as amended, or a decision or ruling of the Secretary of Finance.[17]

In a March 22, 2013 Resolution, the CTA First Division ruled that it has jurisdiction over the nature and subject matter of the instant petition. Since this case was instituted for the Court to review the decision or ruling of the Secretary of Finance dated November 15, 2011 that affirmed the ruling of the CIR in BIR Ruling No. ITAD 210-11 dated August 15, 2011, the Court needs only to refrain from ruling over the issues on the validity or constitutionality of the RMO. Hence, respondents' Motions to Dismiss were denied for lack of merit.[18]

Both the Secretary of Finance and the CIR filed their Motions for Reconsideration but were denied in the Resolution promulgated on July 3, 2013.[19]

Meanwhile, in view of Administrative Circular No. 01-2013 dated March 26, 2013, reorganizing the three Divisions of the CTA, and the Order of the CTA First Division dated April 5, 2013, this case was transferred to the CTA Third Division.[20]

On September 5, 2013, when the case was called for the initial presentation of evidence for ERO S.A., counsels for the Secretary of Finance and the CIR moved for the suspension of the proceedings on the ground that they filed a Petition for Certiorari with the Supreme Court to annul the March 22, 2013 Resolution.[21]

On September 10, 2013, respondents therein filed a Joint Motion to Suspend the proceedings before the CTA in view of their filing of a Petition for Certiorari (with Urgent Prayer for the Issuance of a Temporary Restraining Order and/or Writ of Preliminary Injunction) with the Supreme Court.[22]

In a September 24, 2013 Resolution, the Court *a quo* granted ERO S.A. fifteen (15) days from notice to file a comment or opposition to the motion and ten (10) days for therein respondents to file their reply.[23]

On October 7, 2013, ERO S.A. filed its Comment[24] and on November 4, 2013 the respondents therein filed their Joint Reply.[25]

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[17] Decision, Rollo, p. 56.
[18] *Id.*
[19] *Id.*
[20] *Id.*
[21] Minutes of Hearing, Division Docket, Vol. I, p. 467.
[22] Division Docket, Vol. I, pp. 498-504.
[23] Division Docket, Vol. II, p. 544.
[24] Division Docket, Vol. II, pp. 545-548.
[25] Division Docket, Vol. II, pp. 550-556.

On November 7, 2013, the Court *a quo* granted the motion and suspended the proceedings in observance of judicial courtesy to the Supreme Court.[26]

In a Resolution dated December 10, 2014,[27] the Supreme Court denied the petition of the Secretary of Finance and the CIR and ruled that the CTA has jurisdiction to hear the case citing *City of Manila v. Judge Grecia-Cuerdo.*[28] The CTA was, therefore, ordered to proceed expeditiously with the proceedings.

On March 23, 2015, the Supreme Court's Resolution dated December 10, 2014 became final and executory.[29]

On July 13, 2015, ERO S.A. filed a Motion to Lift Suspension of Proceedings[30] which the Court *a quo* granted in a July 23, 2015 Resolution.[31]

On September 22, 2015, the Court continued the proceedings but the parties manifested that they would no longer present evidence since the only issue in this case is whether the dividends are subject to the 10% preferential rate. The parties were also given twenty (20) days to file their Joint Stipulation of Facts and Issues.[32]

On October 12, 2015, the parties filed anew their Joint Stipulation of Facts and Issue.[33]

On January 18, 2016, the case was finally deemed submitted for decision after respondents therein submitted their Memoranda on December 2, 2015 and on January 4, 2016, and after petitioner filed its Memorandum on January 4, 2016.[34]

On December 15, 2016, the Court *a quo* rendered a decision which reversed and set aside the ruling of the Secretary of Finance dated November 15, 2011 and BIR Ruling No. ITAD 210-11 dated August 15, 2011.[35]

On May 23, 2017, the Court denied the Motions for Reconsideration of the respondents Secretary of Finance and CIR.[36]

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[26] Resolution, Division Docket, Vol. II, pp. 565-567.
[27] Division Docket, Vol. II, pp. 584-585.
[28] G.R. No. 175723, February 4, 2014.
[29] Entry of Judgment, Division Docket, Vol. II, pp. 575 and 579.
[30] Division Docket, Vol. II, pp. 581-583.
[31] Division Docket, Vol. II, p. 585.
[32] Minutes of September 22, 2018 Hearing, Division Docket, Vol. II, p. 590.
[33] Division Docket, Vol. II, pp. 593-605.
[34] Resolution, Division Docket, Vol. II, p. 711.
[35] Division Docket, Vol. II, pp. 718-737.
[36] Resolution, Division Docket, Vol. II, pp. 770-771.

CTA En Banc Proceedings

On June 13, 2017, the Secretary of Finance filed a Motion for Extension of Time to File Petition for Review and requested for an extension of fifteen (15) days from June 13, 2017, or until June 28, 2017, within which to file the Petition for Review.[37]

The Court *En Banc*, in a Minute Resolution dated June 19, 2017, granted the Secretary of Finance a final and non-extendible period of fifteen (15) days from June 13, 2017, or until June 28, 2017, within which to file the Petition for Review.[38]

On June 28, 2017, the Secretary of Finance filed the Petition for Review.[39]

In a July 17, 2017 Resolution, the Court En Banc ordered respondent ERO S.A. to file its comment[40] which was filed on August 11, 2017.[41]

In an August 24, 2017 Resolution, both parties were ordered to file their memoranda within thirty (30) days from notice.[42]

On November 23, 2017, with the filing of the Memorandum of the Secretary of Finance on October 18, 2017 and that of ERO S.A. on October 19, 2017, the case was deemed submitted for decision.[43]

THE ISSUE

Can ERO S.A., a non-resident foreign corporation, that received dividends from ERO Philippines, its domestic subsidiary, avail of the 10% preferential income tax rate on dividends under the RP-France Tax Treaty?

THIS COURT'S RULING

We resolve to deny the petition and answer the issue in the affirmative.

The facts in this case are not in dispute.

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[37] Rollo, pp. 1-4.
[38] Rollo, p. 30.
[39] Rollo, pp. 31-42.
[40] Rollo, p. 129.
[41] Rollo, pp. 131-133.
[42] Rollo, pp. 135-136.
[43] Resolution, Rollo, pp. 164-165.

In 2010, ERO S.A., a non-resident foreign corporation, received dividends from its subsidiary ERO Philippines. ERO Philippines is a domestic corporation, 99% of whose total issued and outstanding shares are owned by its parent, ERO S.A.[44]

The issue at the core of the case is not novel either. Nonetheless, the petitioner is of the view that because ERO S.A. did not comply with the procedural requirements for the filing of the TTRA on time, under RMO 1-2000 and RMO 72-2010, it cannot avail of the 10% preferential rate on intercompany dividends under RP-France Tax Treaty.

Failure to strictly comply with the prerequisite in RMO 1-2000 or RMO 72-2010 is not fatal to the taxpayer's availment of the preferential rate under a tax treaty.

Article II Section 2 of the 1987 Constitution declares that the Philippines "adopts the generally accepted principles of international law" as part of the law of the land.

Accordingly, under the basic international law principle of *pacta sunt servanda*, the state has the duty to fulfill its treaty obligations in good faith. This entails the harmonization of national legislation with treaty provisions.[45]

The RP-France Tax Treaty is just one among a number of bilateral agreements which the Philippines has entered into for the avoidance of double taxation. The purpose of these tax treaties is "to reconcile the national fiscal legislations of the contracting parties in order to help the taxpayer avoid simultaneous taxation in two different jurisdictions."[46]

The Supreme Court in *Deutsche Bank AG Manila Branch v. Commissioner of Internal Revenue*[47] was confronted with the very issue of whether the failure to strictly comply with RMO 1-2000 will deprive a taxpayer of the benefit of a tax treaty. The Supreme Court clarified that noncompliance with the prerequisite in RMO 1-2000 is *not* fatal to the taxpayer's availment of the preferential rate under a tax treaty.

In fact, it was clearly stated that the application for a tax treaty relief or a TTRA from the BIR should merely operate to *confirm* the entitlement of the taxpayer to the relief. In other words, the basis of the entitlement to the

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[44] Pars. 1, 2, 4 and 6, Stipulated Facts, Joint Stipulation of Facts and Issue, Division Docket, Vol. II, pp. 594-595.
[45] *Commissioner of Internal Revenue v. Pilipinas Shell Petroleum Corporation*, G.R. No. 188497, February 19, 2014.
[46] *Commissioner of Internal Revenue v. SC Johnson and Son, et al.*, G.R. No. 127105, June 25, 1999.
[47] G.R. No. 188550, August 19, 2013.

preferential rate is *not* the confirmatory ruling from the BIR but the Tax Treaty itself. Thus:

> "Likewise, it must be stressed that there is nothing in RMO No. 1-2000 which would indicate a deprivation of entitlement to a tax treaty relief for failure to comply with the 15-day period. We recognize the clear intention of the BIR in implementing RMO No. 1-2000, but the CTA's outright denial of a tax treaty relief for failure to strictly comply with the prescribed period is not in harmony with the objectives of the contracting state to ensure that the benefits granted under tax treaties are enjoyed by duly entitled persons or corporations.
>
> Bearing in mind the rationale of tax treaties, the period of application for the availment of tax treaty relief as required by RMO No. 1-2000 should not operate to divest entitlement to the relief as it would constitute a violation of the duty required by good faith in complying with a tax treaty. The denial of the availment of tax relief for the failure of a taxpayer to apply within the prescribed period under the administrative issuance would impair the value of the tax treaty. At most, the application for a tax treaty relief from the BIR should merely operate to confirm the entitlement of the taxpayer to the relief.
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> The obligation to comply with a tax treaty must take precedence over the objective of RMO No. 1-2000. Logically, noncompliance with tax treaties has negative implications on international relations, and unduly discourages foreign investors. While the consequences sought to be prevented by RMO No. 1-2000 involve an administrative procedure, these may be remedied through other system management processes, e.g., the imposition of a fine or penalty. But we cannot totally deprive those who are entitled to the benefit of a treaty for failure to strictly comply with an administrative issuance requiring prior application for tax treaty relief." (*underscoring supplied*)

In connection with this holding, it must be emphasized that RMO 1-2000 and 72-2010 were issued simply "to streamline the processing of the tax treaty relief application in order to improve efficiency and service to the taxpayers."[48] Beyond the stated purposes of these issuances, nothing is explicitly provided or can reasonably be construed therein that authorizes nullifying, reversing or even modifying the provisions of the RP-France Tax Treaty on intercompany dividends.

Moreover, in harmony with their stated purposes, these RMOs were never intended to modify substantive rights of taxpayers which were recognized and granted under the tax code or tax treaties precisely because, as Revenue Administrative Order (RAO) 1-2003 defines them, they merely serve as instructions that deal with matters of administration or procedures:

[48] Section I of RMO 1-2000 and Section 1 of RMO 72-2010.

"SECTION 3. Classification of BIR Rulings and Issuances. — The following terms shall have the meaning described below:

xxx xxx xxx

h) Revenue Memorandum Orders (RMO) — These are directives or instructions outlining procedures, techniques, methods, processes, operations, activities, work flow, and the like, which are necessary to carry out programs or to achieve policy goals and objectives. These issuances may be of general or of limited scope yet in any case require definite compliance by those concerned. They are not addressed to any particular group of employees or offices because they are for general information, but those directly concerned with the compliance of these provisions are either definitely stated, or unmistakably implied thereat." (*underscoring supplied*)

In other words, the Supreme Court in *Deutsche* has wisely determined that the evil sought to be avoided by RMO 1-2000 and even RMO 72-2010, which is the erroneous application of treaty provisions, is a lesser evil compared to the consequences of the failure to comply with treaty obligations in good faith under international law.

On January 14, 2015, the Supreme Court in the consolidated refund cases of *CBK Power Company Limited v. Commissioner of Internal Revenue*[49] quoted in agreement the holding of *Deutsche*. The cases emphasized the *Deutsche* holding that BIR should *not* impose additional requirements that would remove the availment of the benefit provided for under these bilateral agreements:

"The issue of whether the failure to strictly comply with RMO No. 1-2000 will deprive persons or corporations of the benefit of a tax treaty was squarely addressed in the recent case of *Deutsche Bank AG Manila Branch v. Commissioner of Internal Revenue* (Deutsche Bank), where the Court emphasized that **the obligation to comply with a tax treaty must take precedence over the objective of RMO No. 1-2000**, xxx:

xxx xxx xxx

The objective of RMO No. 1-2000 in requiring the application for treaty relief with the ITAD before a party's availment of the preferential rate under a tax treaty is to avert the consequences of any erroneous interpretation and/or application of treaty provisions, such as claims for refund/credit for overpayment of taxes, or deficiency tax liabilities for underpayment. However, as pointed out in *Deutsche Bank,* the underlying principle of prior application with the BIR becomes **moot in refund cases** – as in the present case – where the very basis of the claim is **erroneous or there is excessive payment** arising from the non-availment of a tax treaty relief at the first instance. Just as Deutsche Bank was not faulted by the Court for not complying with RMO No. 1-2000 prior to the transaction, so should CBK Power. In parallel, CBK Power could not have applied for a

[49] G.R. Nos. 193383-84 and 193407-08, January 14, 2015.

tax treaty relief 15 days prior to its payment of the final withholding tax on the interest paid to its lenders **precisely because it erroneously paid said tax** on the basis of the regular rate as prescribed by the NIRC, and not on the preferential tax rate provided under the different treaties. As stressed by the Court, the prior application requirement under RMO No. 1-2000 then becomes **illogical.**

Not only is the requirement illogical, but it is also an imposition that is **not found at all in the applicable tax treaties.** In *Deutsche Bank*, the Court categorically held that the BIR should not impose additional requirements that would negate the availment of the reliefs provided for under international agreements, especially since said tax treaties do not provide for any prerequisite at all for the availment of the benefits under said agreements.

It bears reiterating that the application for a tax treaty relief from the BIR should **merely operate to confirm** the entitlement of the taxpayer to the relief. xxx." (*underscoring supplied and citations omitted*)

In the recent case of *Air Canada v. Commissioner of Internal Revenue*,[50] the Supreme Court again invoked the principle of *pacta sunt servanda* and underscored the precedence of tax treaties over mere BIR administrative issuances by quoting *Deutsche* at length:

"Observance of any treaty obligation binding upon the government of the Philippines is anchored on the constitutional provision that the Philippines 'adopts the generally accepted principles of international law as part of the law of the land[.]' *Pacta sunt servanda* is a fundamental international law principle that requires agreeing parties to comply with their treaty obligations in good faith.

Hence, the application of the provisions of the National Internal Revenue Code must be subject to the provisions of tax treaties entered into by the Philippines with foreign countries.

In *Deutsche Bank AG Manila Branch v. Commissioner of Internal Revenue*, this court stressed the binding effects of tax treaties. It dealt with the issue of 'whether the failure to strictly comply with [Revenue Memorandum Order] RMO No. 1-2000 will deprive persons or corporations of the benefit of a tax treaty.' Upholding the tax treaty over the administrative issuance, this court reasoned thus:

xxx xxx xxx"
(*underscoring supplied and citations omitted*)

Finally, it bears stressing that, in the case at bench, there was in fact a TTRA filed with the ITAD[51] by ERO S.A. However, the CIR deemed the same as filed beyond the period required under RMO 1-2000 and RMO 72-

[50] G.R. No. 169507, January 11, 2016.
[51] Par. 6, Stipulated Facts, Joint Stipulation of Facts and Issue, Division Docket, Vol. II, p. 595.

2010.[52] Surely, consistent with the reasoning in *Deutsche* and *CBK* cases, ERO S.A.'s failure to strictly comply with the RMO cannot be deemed as sufficient justification to negate the application of the RP-France Tax Treaty to the dividend payments it received from ERO Philippines. The courts cannot countenance administrative issuances that override, instead of remaining consistent and in harmony with, the law they seek to apply and implement.[53]

Under the RP-France Tax Treaty, the dividends received by ERO S.A. from ERO Philippines are subject to 10% preferential rate.

As a general rule, gross income received in 2010 by a non-resident foreign corporation from all sources within the Philippines are taxed 30% under Section 28(B)(1) of the 1997 NIRC, as amended:

> "**SEC. 28.** *Rates of Income Tax on Foreign Corporations.* -
>
> xxx xxx xxx
>
> (B) Tax on Nonresident Foreign Corporation. –
>
> (1) *In General.* - Except as otherwise provided in this Code, a foreign corporation not engaged in trade or business in the Philippines shall pay a tax equal to thirty-five percent (35%) of the gross income received during each taxable year from all sources within the Philippines, such as interests, dividends, rents, royalties, salaries, premiums (except reinsurance premiums), annuities, emoluments or other fixed or determinable annual, periodic or casual gains, profits and income, and capital gains, except capital gains subject to tax under subparagraphs (C) and (d): *Provided,* That effective January 1, 2009, the rate of income tax shall be thirty percent (30%).
>
> xxx xxx xxx"

However, under Section 28(B)(5)(b) of the same law, intercorporate dividends are taxed 15% provided that the country in which the recipient corporation is domiciled allows a 15% credit against the tax due from the corporation which is deemed to have been paid in the Philippines:

> "(5) *Tax on Certain Incomes Received by a Nonresident Foreign Corporation.* –
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> xxx xxx xxx

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[52] Petition for Review, Rollo, pp. 39-41.

[53] *Philippine Bank of Communications v. Commissioner of Internal Revenue, et al.*, G.R. No. 112024, January 28, 1999.

> (b) *Intercorporate Dividends.* - A final withholding tax at the rate of fifteen percent (15%) is hereby imposed on the amount of cash and/or property dividends received from a domestic corporation, which shall be collected and paid as provided in Section 57(A) of this Code, subject to the condition that the country in which the nonresident foreign corporation is domiciled, shall allow a credit against the tax due from the nonresident foreign corporation taxes deemed to have been paid in the Philippines equivalent to twenty percent (20%), which represents the difference between the regular income tax of thirty-five percent (35%) and the fifteen (15%) percent on dividends as provided in this subparagraph: *Provided*, that effective January 1, 2009, the credit against the tax due shall be equivalent to fifteen percent (15%) tax on dividends;" (*underscoring supplied*)

Pursuant to Article 10 of the RP-France Tax Treaty signed on January 9, 1976, ERO S.A. as resident of France can be taxed 15% on dividends paid by ERO Philippines, a domestic corporation, of which the former owns 99% of the total issued and outstanding shares:

> "CONVENTION BETWEEN THE GOVERNMENT OF THE REPUBLIC OF THE PHILIPPINES AND THE GOVERNMENT OF THE FRENCH REPUBLIC FOR THE AVOIDANCE OF DOUBLE TAXATION AND THE PREVENTION OF FISCAL EVASION WITH RESPECT TO TAXES ON INCOME
>
> The Government of the Republic of the Philippines and the Government of the French Republic,
>
> Desiring to conclude a Convention for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income, with a view in particular to encourage international trade and investment,
>
> Have agreed as follows:
>
> xxx xxx xxx
>
> **ARTICLE 10**
>
> *Dividends*
>
> 1. Dividends paid by a company which is a resident of a Contracting State to a resident of the other Contracting State may be taxed in that other State.
>
> 2. However, such dividends may be taxed in the Contracting State of which the company paying the dividends is a resident, and according to the law of that State, but if the recipient is the beneficial owner of the dividends the tax so charged shall not exceed: Ju

a) 15 per cent of the gross amount of the dividends if the recipient is a company (excluding partnership) which holds directly at least 10 per cent of the voting shares of the company paying the dividends;

b) in all other cases, 25 per cent of the gross amount of the dividends.

This paragraph shall not affect the taxation of the company in respect of the profits out of which the dividends are paid.

3. The term "dividends" as used in this Article means income from shares, "jouissance" shares or "jouissance" rights, mining shares, founders' shares or other rights, not being debt-claims, participating in profits, as well as income from other corporate rights which is subjected to the same taxation treatment as income from shares by the taxation law of the State of which the company making the distribution is a resident.

4. The provisions of paragraphs 1 and 2 shall not apply if the recipient of the dividends, being a resident of a Contracting State, carries on business in the other Contracting State of which the company paying the dividends is a resident, through a permanent establishment situated therein, or performs in that other State professional services from a fixed base situated therein and the holding in respect of which the dividends are paid is effectively connected with such permanent establishment or fixed base. In such a case the provisions of Article 7 or Article 14, as the case may be, shall apply.

5. A resident of the Philippines who receives dividends paid by a company which is a resident of France may obtain the refund of the prepayment (precompte) relating to such dividends, in the event it had been paid by the distributing company. Such prepayment (precompte) shall be refunded subject to the deduction of the tax levied according to the French taxation law and the provisions of paragraph 2.

The gross amount of the prepayment (precompte) refunded shall be deemed to be dividends for the purposes of the provisions of this Convention.

6. Where a company resident of a Contracting State has in the other Contracting State a permanent establishment, the profits of its permanent establishment shall, after having borne the corporation tax, be liable to a tax the rate of which shall not exceed 15 per cent, according to the laws of that other Contracting State." (*underscoring supplied*)

The 15% preferential rate was, nevertheless, subsequently reduced to 10% in a June 26, 1995 protocol to the treaty:

"PROTOCOL TO THE TAX CONVENTION BETWEEN THE GOVERNMENT OF THE REPUBLIC OF THE PHILIPPINES AND THE GOVERNMENT OF THE FRENCH REPUBLIC SIGNED ON JANUARY 9, 1976

> The Government of the Republic of the Philippines and the Government of the French Republic, desiring to amend the Convention signed on January 9, 1976 between the two Governments for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income (hereinafter referred to as 'the Convention'), have agreed as follows:
>
> xxx xxx xxx
>
> ARTICLE 5
>
> In Article 10 of the Convention:
>
> — <u>in paragraph 2, the rates of '15 percent' and '25 percent' are replaced respectively by '10 percent' and '15 percent';</u>
>
> — in paragraph 6, the rate of '15 percent' is replaced by '10 percent'." (*underscoring supplied*)

Considering the foregoing discussions, the Court *a quo*, therefore, correctly held that ER S.A. is qualified to avail of the 10% preferential rate on dividends received from ERO Philippines on May 6, 2010 and on August 31, 2010. Petitioner has failed to muster any legal basis against the settled jurisprudence and to surmount the holding of the Court *a quo* reversing the ruling of the petitioner Secretary of Finance dated November 15, 2011 and BIR Ruling No. ITAD 210-11 dated August 15, 2011.

WHEREFORE, premises considered, the Petition for Review is **DENIED** for lack of merit. The December 15, 2016 Decision and the May 23, 2017 Resolution are hereby **AFFIRMED**.

SO ORDERED.

JUANITO C. CASTAÑEDA, JR.
Associate Justice

WE CONCUR:

ROMAN G. DEL ROSARIO
Presiding Justice

(On Leave)
ERLINDA P. UY
Associate Justice

(On Leave)
ESPERANZA R. FABON-VICTORINO
Associate Justice

Cielito N. Mindaro-Grulla
CIELITO N. MINDARO-GRULLA
Associate Justice

MA. BELEN M. RINGPIS-LIBAN
Associate Justice

Catherine T. Manahan
CATHERINE T. MANAHAN
Associate Justice

CERTIFICATION

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

ROMAN G. DEL ROSARIO
Presiding Justice