REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

EN BANC

****

ISLAND POWER CORPORATION
Petitioner,

- versus -

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

C.T.A. EB No. 26
(C.T.A. Case No. 5922)

Members:
ACOSTA, *P.J.*
CASTAÑEDA, JR.,
BAUTISTA,
UY,
CASANOVA, and
PALANCA-ENRIQUEZ, *JJ.*

Promulgated:

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DECISION

UY, J.:

This is a Petition for Review before the Court of Tax Appeals *En Banc* filed on September 14, 2004 under Republic Act No. 9282, seeking a review of the Decision and Resolution by the then Court of Tax Appeals, which under Republic Act No. 9282, is now a Division of the current Court of Tax Appeals, in CTA Case No. 5922, entitled "Island Power Corporation vs. Commissioner of Internal Revenue", to wit:

1.) Decision promulgated on May 17, 2004 denying petitioner's petition for review for lack of merit, upholding Assessment Notice No. 000292 and ordering petitioner to pay the respondent the amount of P63,097,199.81 representing deficiency withholding tax for taxable year 1995, inclusive of interest. In addition, petitioner was ordered to pay the respondent 20% delinquency interest from October 14, 1998 until full payment pursuant to Section 249 (a)(c)(3) of the old Tax Code; and

2.) Resolution promulgated on August 18, 2004 denying petitioner's Motion for Reconsideration of the aforesaid decision.

The established facts as contained in the assailed Decision are as follows:

"Petitioner is a corporation duly established and registered under the laws of the Republic of the Philippines. It is engaged in the business of power generation *(par. 1, Joint Stipulation of Facts).*

On December 21, 1993, a contract was entered into between petitioner Island Power Corporation and Edison Global Electric Ltd. *(Edison, for brevity)*, denominated as "Contract for the Engineering, Supply, Delivery (CIF Site) Construction, Erection, Testing and Commissioning (Turn-Key) of Total of 7 MW Two (2) Units Enterprise DSR-48 Electric Generator Sets at San Jose, Occidental Mindoro, Philippines," for a total contract price of P118,036,870.00 *(Exhs. G-G-15; Exh. 9).*

On April 15, 1996, petitioner filed its Annual Income Tax reporting a 'nil' taxable income as it was still in its pre-operating stage *(Exh. 2).*

On March 5, 1998, petitioner received a letter from respondent, informing it that inasmuch as it has not reported an income from 1993 to 1995 taxable years and failed to withhold 35% on the fees/income paid to Edison Global Electric, Ltd., it is held liable for violation of Section 53(b)(2) [now 50] of the Tax Code, in relation to Section 25(b)(1) of the same Code.

On December 15, 1998, petitioner received Assessment Notice No. 000292 dated September 14, 1998 involving the aggregate amount of P63,097,199.81 for Deficiency Withholding Tax and Interest covering the period 1995, details of which are shown below *(Exh. B)*:

Withholding Tax

Tax Due	P41,312,905.00
Add: Interest 1/25/96 to 9/14/98	21,784,294.81
Total Amount Payable	P63,097,199.81

On January 14, 1999, petitioner filed its letter-protest dated December 23, 1998, with the Assessment Division of Revenue Region No. 7 *(Exh. C)*, claiming that it does not have any obligation to withhold 35% of its payment to Edison because Sections 50(a) and 25(b)(1) of the NIRC is inapplicable to Edison, the latter being a 'resident foreign corporation.'

A Preliminary Collection Letter dated March 29, 1999 was subsequently issued by respondent for the payment of petitioner's deficiency withholding tax including interest *(Exh. D)*. For failure on the part of petitioner to reply to the Preliminary Collection Letter, a Final Notice Before Seizure was then issued by respondent on April 22, 1999 *(Exh. E)*, which was received by petitioner on April 30, 1999.

On May 6, 1999, petitioner filed its reply letter dated May 3, 1999 and alleged that a protest letter questioning the subject assessment was filed but which has not yet been resolved *(Exh. F)*; hence, the issuance of the "Preliminary Collection Letter" and the "Final Notice Before Seizure" was premature as the assessment has not yet become final.

On July 30, 1998, petitioner received a letter from the Collection Division of Revenue Region No. 7 *(Exh. I)*, denying petitioner's protest on the ground that petitioner failed to dispute the correctness of the assessment within the 30-day reglementary period. Thus, the assessment had allegedly become final and executory.

On August 12, 1999, petitioner appealed the denial of its protest by filing the instant petition for review. (Decision, C.T.A. Case No. 5922, pp.1-3)."

On May 17, 2004, the petition for review in C.T.A. Case No. 5922 was denied for lack of merit, as well as petitioner's motion for reconsideration of said denial on August 18, 2004. Thus, petitioner filed this Petition for Review before the Court of Tax Appeals *En Banc* on September 14, 2004 raising the following grounds:

I.

THE HONORABLE COURT OF TAX APPEALS (DIVISION) MISAPPRECIATED THE EVIDENCE PRESENTED BY PETITIONER;

II.

THE HONORABLE COURT OF TAX APPEALS (DIVISION) ERRED IN DECLARING THAT EDISON GLOBAL ELECTRIC LTD. MERELY ENGAGED IN AN ISOLATED TRANSACTION WHICH DID NOT CONSTITUTE "DOING BUSINESS" WITHIN THE MEANING OF THE LAW;

III.

PETITIONER IS NOT LIABLE FOR DEFICIENCY WITHHOLDING TAX AND INTEREST.

Petitioner contends that Edison Global Electric Ltd. (EGE or EDGE for short), is a resident foreign corporation directly liable for a thirty five (35%) percent tax on its taxable income derived from all sources within the Philippines, including the contract price that petitioner paid EDGE for the construction of its San Jose, Occidental Mindoro power plant because EDGE is engaged in trade or business within the Philippines. However, petitioner claims that the Court of Tax Appeals (Division) relied heavily on the fact that it had only one contract with EDGE and on this sole basis, it allegedly made the erroneous pronouncement that EDGE was only engaged in an "isolated transaction" there having been no showing that it continued its business operations in the Philippines even after the completion of the construction of the power plant.

Petitioner argues that the following are indications that EDGE is "doing business" in the Philippines : the enormity and cost of building one power plant in San Jose, Occidental Mindoro, which was more than four million U.S. dollars; the stipulation in its Turn Key Contract with EDGE providing credit terms to petitioner including payment through a letter of credit of about half the total amount of the contract price; the provision that EDGE's personnel would extend full cooperation to petitioner and if in case petitioner would not be able to complete the project, EDGE had an option to take over and complete the project on its own; EDGE, through its representative, David Tan, based on his travel records, stayed in the Philippines for a period of more than one hundred eighty (180) days and the duration of its project with petitioner lasted for more than one year, constitutes "doing business" in accordance with the provisions of the Foreign Investment Act (Section 3, of R.A. No. 7042); the maintenance of a post office box, contact telephone and telefax numbers as a "correspondent point" in the Philippines by EDGE and the testimony of petitioner's witness, Engineer Francisco Delgado, that the Philippine office address of EDGE as appearing in a letter dated January 25, 1995, was located at the 27th Floor, Tektite Bldg., Ortigas Center, Pasig City and that it designated one of its employee-electrical engineers as its site manager.

On the other hand, respondent, in scrutinizing the contract between the petitioner and EDGE cites the cases of Mentholatum Co. Inc., et al. v. Mangaliman (*72 Phil 524, 1941*) and Agilent Technologies Singapore (Pte.) Ltd. v. Integrated Silicon Technology Philippines Corporation (*427 SCRA 593,2004)*, and submits that the Supreme Court discoursed on the two general tests, the substance test and continuity test, to determine whether or not a foreign corporation can be considered as "doing business" in the Philippines.

It is respondent's theory that EDGE had engaged in an isolated contract to sell and construct a power plant for petitioner including the auxiliary services necessary to activate the plant; that upon completion of the heavy fuel oil power plant at San Jose, Occidental Mindoro, ready and complete for commercial operation, EDGE will cease to engage in its main line of business in the Philippines. Hence, the outcome is not deemed "doing business" under the substance test, that is, 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.

As to the continuity test, respondent maintains that 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 organizations, and that petitioner failed to substantiate the existence of continuous commercial dealings of EDGE after carrying out the San Jose power plant project. There was allegedly no showing that the channels of communications and other office facilities referred to by petitioner in dealing with EDGE were utilized by the latter in connection with other power plant construction, sales or projects within the Philippines. Thus, petitioner allegedly failed to prove the existence of continuous commercial dealings or arrangements by EDGE sufficient to constitute "doing business" in the Philippines.

Based on the parties' respective allegations and assertions, the issues are: whether or not EDGE is "doing business" as a resident foreign corporation within the purview of the 1977 National Internal Revenue Code and related laws; and whether petitioner is liable for the assessed deficiency withholding tax inclusive of interest for the year 1995 in the amount of P63,097,199.81?

There is no doubt that under Section 25(b)(1) of the 1977 National Internal Revenue Code (NIRC), a non-resident corporation is liable to pay a tax equal to thirty five (35%) percent of the gross income received during each taxable year from all sources within the Philippines. To quote:

"SECTION 25. ***Rates of tax on foreign corporation.*** —

(a) ***Tax on resident foreign corporations*** (1) *In general.* — Unless otherwise provided, a corporation organized, authorized, or existing under the laws of any foreign country, engaged in trade or business within the Philippines, shall be subject to a tax equivalent to 35% of the taxable income derived in the preceding taxable year from all sources within the Philippines.

xxx xxx xxx

(b) ***Non-resident foreign corporations.*** — (1) *In general.* — Unless otherwise provided, a foreign corporation not engaged in trade or business in the Philippines shall pay a tax equal to 35% of the gross income received during each taxable year from all sources within the Philippines such as interest, dividends, rents, royalties, salaries, premiums (except reinsurance premiums), annuities, emoluments or other fixed or determinable annual, periodical or casual gains, profits and income, and capital gains, except capital gains subject to tax under sub-paragraph 5 (C)."

Material to the resolution of the controversy in this case is the determination of what is a resident foreign corporation and a non-resident foreign corporation. Under Section 20 (h) and (i) of the 1977 NIRC, as amended (now Section 20 (H) and (I) of the 1997 National Internal Revenue Code), the terms resident foreign corporation and non-resident corporation are distinguished from each other in the following manner:

"Sec. 20. Definitions. — xxx

xxx xxx xxx

(h) The term "resident foreign corporation" applies to a foreign corporation engaged in trade or business within the Philippines.

(i) The term "non-resident foreign corporation" applies to a foreign corporation not engaged in trade or business within the Philippines.

Correspondingly, a definitive classification of EDGE's tax personality, either as a resident or non-resident foreign corporation, will validate or invalidate the assessment made by respondent against petitioner for non-payment of withholding tax at 35% of the total amount of P118,036,870.00 for services rendered by EDGE in favor of the petitioner pursuant to Section 50 (a) of the 1977 NIRC, as amended. We quote:

"SEC. 50. ***Withholding of Tax at Source.***

a) ***Withholding of final tax on certain incomes.*** – The tax imposed or prescribed by Sections 21 (c), 21 (d) (2), 22 (a) (2), (b), (c), (d), (e); 24 (e) (1), (e) (2) (B), (e) (3); and 25 (a) (4), (a) (5), (a) (6) (A), (a) (6) (B), (C) (ii), (b) (1); (b) (2), (b) (3), (b) (4), (b) (5) (A), (b) (5) (B), (m) (5) (C) (ii) of this Code on specified items of income shall be withheld by payor-corporation and/or person and paid in the same manner and subject to the same conditions as provided in Section 51 of the National Internal Revenue Code, as amended."

As to whether or not EDGE was "doing business" in the Philippines as to be considered a "resident foreign corporation", the assailed Decision already elaborated in this wise:

"The phrase 'doing business' has been interpreted by the Supreme Court in the case of ***The Mentholatum Co., Inc. vs. Mangaliman*, 72 Phil. 524** and we quote:

'No general rule or governing principles can be laid down as to what constitutes "doing" or "engaging in" or "transacting" business. Indeed, each case must be judged in the light of its peculiar environmental circumstances. 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 Internal 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.'

Moreover, in the case of ***ABB Power Generation Ltd. vs. Commissioner of Internal Revenue*, CTA Case No. 4888, February 6, 1996,** this court, citing the case of ***Pacific Micronesian Line, Inc. vs. Del Rosario and Pelingon*, 96 Phil. 30** passed upon the issue in this wise:

'It is a rule generally accepted that one single or isolated business transaction does not constitute 'doing business' within the meaning of the law, and that transactions which are occasional, incidental and casual, that of a character to indicate a purpose to engage in business do not constitute the doing or engaging in business contemplated by law. In order that a foreign corporation may be regarded as doing business in a State, there must be continuity of conduct and intention to establish a continuous business, such as the appointment of a local agent, and not one of a temporary character.'

This court believes that the letter dated January 25, 1995 *(Exh. H)* addressed to petitioner did not prove that Edison was doing business in the Philippines. While the address of the alleged Philippine office of Edison was printed at the lower right portion of the letter, it did not, however, establish the fact that it actually maintained a branch office in the Philippines. It is not even a business address. P.O. Box 12290, Ortigas Center, Pasig, Metro Manila is a postal office address.

Moreover, the travel records of Mr. David C. Tan relative to his Philippine travels merely showed that he came to the Philippines and Hongkong during the period March 7, 1994 to September 2, 1996. There was, however, no other document to show proof that his various travels to the Philippines during the said period were incurred in furtherance of the Contract entered into with herein petitioner, that is, for the purpose of the construction of the power plant in Occidental Mindoro.

While Edison completed the construction of the power plant in Occidental Mindoro after almost two years (the construction of the power plant commenced in January 1994 and was completed in September 1995) *[pp. 20-25, TSN, January 29, 2001]*, Edison cannot be considered as doing business in the Philippines as there was no clear and convincing proof that it continued its business operations in the Philippines even after the completion of the construction of the power plant. It is, thus, considered, as engaged in an 'isolated transaction' which does not constitute 'doing business' within the meaning of the law.

In other words, petitioner failed to present any clear and convincing proof that Edison is a resident foreign corporation. Assuming *arguendo* that Edison is in fact a resident foreign corporation, **petitioner could have easily presented the Income Tax Return of Edison which is a vital document to prove that it is, indeed, a resident foreign corporation**. This court cannot rule on this issue on mere assumptions and conjectures. Failure on the part of petitioner to establish such fact, this court cannot consider Edison as a resident foreign corporation. Thus, the imposition of the 35% tax rate on the income payments made by petitioner to Edison was proper (*Emphasis supplied).*"

To emphasize, the application of the meaning of "transacting business" or "doing business" is a question of fact. The current jurisprudence reveals that each case must be adjudged in view of the idiosyncratic state of affairs of the corporation within the jurisdiction of the Philippines. All the combined acts of the foreign corporation in the state must be considered, and every circumstance is material, which indicates a purpose on the part of the corporation to engage in some part of its regular business. ***(Pacific Micronesian Line, Inc. vs. Del Rosario, 96 Phil. 23 [1954])***.

The contract between the petitioner and Edison shows that the latter's undertaking was limited to the construction of a single heavy fuel oil-fed seven (7) megawatt power plant at San Jose, Occidental Mindoro; that Edison would build the plant until it was complete and ready for commercial operation and that Edison would sell the commissioned plant to petitioner. Thereafter, petitioner would operate the power plant to sell electricity to the Occidental Mindoro Electric Cooperative. More importantly, and as already held in the assailed Decision, petitioner failed to adduce any clear and convincing evidence that Edison subsequently built and commissioned other power plants in the Philippines. Petitioner could have easily presented Edison's Philippine income tax return to prove that it is a resident foreign corporation. Although it was stipulated in the contract that more than half of the price of the power plant would be paid by a letter of credit, such credit accommodation was a mere incident involved in the carrying out of Edison's basic undertaking to build and sell a power plant to petitioner.

Contrary to petitioner's assertion, said credit transaction is not proof of continuity of commercial dealings in the Philippines. Neither is the mere enormity of the financial outlay of the project a determining factor that EDGE was "doing business" in the Philippines.

Finally, respondent is correct in saying that maintaining a post office box and phone numbers, constituting channels for Edison's correspondence and other communications, as well as the alleged possession of an office in the Ortigas Center Complex, do not imply a continuity of a foreign corporation's commercial dealings or arrangements in the Philippines. In fact, it appears that these channels and office facilities were utilized by Edison only in the context of carrying out the San Jose power plant project as no further evidence was presented to show that these channels and office facilities were also utilized by Edison in connection with other power plant construction/sale projects in the Philippines.

All the foregoing considered, the Court En Banc finds no merit in the instant petition. We agree with the respondent that Edison had engaged in an isolated contract to sell and construct a power plant for petitioner, together with the auxiliary services necessary to activate the plant, for eventual turnover to petitioner as commercial operator thereof. Thus, Edison was not "doing business" in the Philippines within the contemplation of the law and is therefore, a non-resident foreign corporation liable to pay 35% on its gross income received during each taxable year from all sources within the Philippines and petitioner is liable to pay deficiency withholding tax for the taxable year 1995, inclusive of interest, assessed against it by respondent Commissioner arising from its Turn Key Contract with Edison.

WHEREFORE, the instant petition is hereby **DENIED** due course, and accordingly **DISMISSED** for lack of merit. Accordingly, the assailed Decision dated May 17, 2004 and the Resolution dated August 18, 2004 are **AFFIRMED**.

ERLINDA P. UY
Associate Justice

WE CONCUR:

ERNESTO D. ACOSTA
Presiding Justice

JUANITO C. CASTAÑEDA, JR.
Associate Justice

(On Official Leave)
LOVELL R. BAUTISTA
Associate Justice

CAESAR A. CASANOVA
Associate Justice

OLGA PALANCA-ENRIQUEZ
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 *En Banc*.

ERNESTO D. ACOSTA
Presiding Justice