**REPUBLIC OF THE PHILIPPINES**
**COURT OF TAX APPEALS**
**QUEZON CITY**

**MIRANT (PHILIPPINES) OPERATIONS CORPORATION,**
Petitioner,

- versus -

C.T.A. CASE NO. 6382

**COMMISSIONER OF INTERNAL REVENUE,**
Respondent.

**Promulgated:**
MAY 27 2004

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# DECISION

This case involves a claim for refund or issuance of a tax credit certificate representing allegedly erroneously paid final withholding taxes for the month of December 1999 in the amount of P3,206,268.17 and various months of calendar year ending December 31, 2000 in the amount of P16,882,167.61 or in the aggregate amount of **TWENTY MILLION EIGHTY EIGHT THOUSAND FOUR HUNDRED THIRTY FIVE AND 78/100 PESOS (P20,088,435.78).**

Petitioner Mirant (Philippines) Operations Corporation (MPOC) [formerly Southern Energy Asia-Pacific Operations (Phils), Inc.], is a domestic corporation duly organized and existing under and by virtue of the laws of the Republic of the Philippines. It is primarily engaged in the business of designing, constructing, erecting, assembling, commissioning, operating, maintaining, rehabilitating and managing gas turbine and other power generating plants and related facilities for the conversion into electricity of coal, distillate and other fuel provided by and under contract with the Government of the Republic of the Philippines, or any subdivision, instrumentality or agency thereof, or any government owned or controlled corporations or other entity engaged in the development, supply or distribution of energy. Its principal office address is located at

Barangay Ibabang Pulo, Pagbilao Grande Island, Pagbilao, Quezon Province (*pars 1 & 3, Joint Stipulation of Facts & Restatement of Issues).*

Prior to petitioner's name as MPOC, it was originally registered as Hopewell Tileman Project Management Corporation with the Securities and Exchange Commission and was issued SEC Registration No. AS093-04117 on May 31, 1993. On March 24, 1994, it registered itself as a withholding agent of the Bureau of Internal Revenue and was subsequently issued Taxpayer's Identification Number 003-057-796. (*pars 4 & 5, Joint Stipulation of Facts & Restatement of Issues).*

On July 29, 1994, petitioner amended its corporate name Hopewell Tileman Project Management Corporation to CEPA Tileman Project Management Corporation. On November 21, 1997, its Articles of Incorporation was again amended to adopt a new corporate name, CEPA Operations (Philippines) Corporation. Furthermore, on November 24, 2000, petitioner filed its Amended Articles of Incorporation to change its corporate name to Southern Energy Asia-Pacific Operations (Philippines) Inc.. Finally, on April 30, 2001, its corporate name was amended to Mirant (Philippines) Operations Corporation (MPOC). However, it is to be noted that petitioner's TIN 003-057-796 remained the same (*pars 6-13, Joint Stipulation of Facts and Restatement of Issues*).

On January 25, 2000, petitioner, then under the corporate name CEPA Operations (Philippines) Corporation, filed its Monthly Remittance Return of Income Taxes Withheld for the period December 1999 reflecting an amount of P3,206,268.17 as final taxes withheld from VHL Enterprises *(Exhibit A-4)* with details as follows:

| Period Covered | Income Payment | Rate (%) | FWT |
|---|---|---|---|
| December 1999 | 4,204,161.67 | 33 | 1,386,373.35 |
| December 1999 | 5,511,802.48 | 33 | 1,818,894.82 |
| **TOTAL** | **9,715,964.15** | | **3,206,268.17** |

The final withholding tax for December 1999 was paid on January 25, 2000 as evidenced by Revenue Official Receipt No. 01333289 reflecting a total amount of P3,218,196.76 in full payment of final and expanded withholding taxes due for December 1999 *(Exhibit B)*.

For the calendar year ending December 31, 2000, petitioner, still under the name of CEPA Corporations (Philippines) Corporation, however, subsequently amended to Southern Energy Asia-Pacific Operations (Philippines), Inc., withheld the total amount of Sixteen Million Eight Hundred Eighty Two Thousand One Hundred Sixty Seven and 61/100 Pesos (P16,882,167.61) as final taxes from its income payments made to VHL Enterprises and WES World-wide Education Service Ltd, both foreign corporations with head offices in Alabama, USA and England, UK, respectively. The details of the final withholding tax remitted and paid are as follows:

| Income Recipient | Period Covered | Income Payment | Rate (%) | FWT |
|---|---|---|---|---|
| VHL Enterprises | February 2000 | 2,379,533.31 | 32 | 761,450.66 |
| VHL Enterprises | February 2000 | 4,617,174.00 | 32 | 1,477,495.68 |
| VHL Enterprises | February 2000 | 4,704,486.75 | 32 | 1,505,435.76 |
| VHL Enterprises | March 2000 | 4,409,905.69 | 32 | 1,411,169.82 |
| VHL Enterprises | May 2000 | 3,436,248.21 | 32 | 1,099,599.43 |
| VHL Enterprises | May 2000 | 4,662,281.13 | 32 | 1,491,929.96 |
| VHL Enterprises | June 2000 | 3,552,938.06 | 32 | 1,136,940.18 |
| VHL Enterprises | July 2000 | 4,445,165.56 | 32 | 1,422,452.98 |
| VHL Enterprises | August 2000 | 5,665,136.06 | 32 | 1,812,843.54 |
| VHL Enterprises | October 2000 | 6,150,371.42 | 32 | 1,968,118.85 |
| WES World-Wide Education ServiceLtd | October 2000 | 527,778.07 | 32 | 168,888.98 |
| VHL Enterprises | November 2000 | 3,549,616.54 | 32 | 1,135,877.29 |
| VHL Enterprises | December 2000 | 4,656,138.99 | 32 | 1,489,964.48 |
| **TOTAL** | | **52,756,773.79** | | **16,882,167.61** |

*(Exhibits H, H-1, H-2, I, I-1, I-2, K, K-1, K-2, L, L-1, L-2, M, M-1, M-2, N, N-1, N-2, P, P-1, P-2, Q, Q-1, Q-2, R, R-1, R-2)*

On December 18, 2001, petitioner, believing that it had erroneously withheld and remitted the above final withholding taxes instead of the 5% expanded/creditable withholding taxes, immediately availed of the Bureau of Internal Revenue's Voluntary

Assessment Program (VAP), and consequently filed and remitted the amount of One Million Seven Hundred Forty Three Thousand Four Hundred Thirty Eight and 25/100 (P1,743,438.25) for VHL Enterprises, and Three Million One Hundred One Thousand Six Hundred Forty Three and 84/100 (P3,101,643.84) for WES World-wide Education Service, Ltd., as expanded/creditable withholding taxes (*par. 17, Joint Stipulation of Facts and Restatement of Issues; Exhibits F, GG & HH).*

Subsequently, on January 23, 2002, petitioner filed an administrative claim for refund with the Bureau of Internal Revenue – RDO 60, Tayabas, Quezon, in the total amount of Twenty Million Eighty Eight Thousand Four Hundred Thirty Five and 78/100 (P20,088,435.78), representing the allegedly erroneously withheld and remitted final taxes for December 1999 and various months of year 2000 *(par. 18, Joint Stipulation of Facts and Restatement of Issues; Exhibits F & GG, HH).*

Without waiting for any response from the respondent, and before it could be barred by prescription, petitioner filed this Petition for Review with this court on January 24, 2002.

Respondent's Answer was filed on February 26, 2002, and by way of his Special and Affirmative Defenses, respondent submitted that:

4. Petitioner's alleged claim for refund is subject to administrative routinary investigation/examination by the Bureau;

5. Petitioner miserably failed to demonstrate that the taxes subject of the case at bar were erroneously or illegally collected;

6. The amount of P20,088,435.78 being claimed by petitioner as alleged erroneously paid final withholding tax for the period December 1999 and calendar year ended December 2000 was not properly documented;

7. Taxes paid and collected are presumed to have been made in accordance with law and regulations, hence, nor refundable;

8. In an action for refund the burden of proof is on the taxpayer to establish its right to refund, and failure to sustain the burden, is fatal to the claim for refund/credit;

9. It is incumbent upon petitioner to show that it has complied with the provisions of Sections 204 (c) and 229 of the Tax Code on the prescriptive period for claiming tax refund/credit;

10. Well-settled is the rule that claims for tax refund/credit are construed in strictissimi juris against the taxpayer as it partakes the nature of exemption from tax and it is incumbent upon the petitioner to show that it is entitled thereto under the law.

Petitioner rested its case sans any evidence from the respondent. Both parties having filed their respective memorandum, this case was then submitted for decision on February 9, 2004.

Petitioner and respondent mutually agreed to the following stipulated issues:

1. Whether or not petitioner has erroneously paid final withholding tax in the amount of P3,206,268.17 for the period December 1999 and P16,882,167.61 for various months of the year 2000 for the total amount of P20,088,435.78;

2. Whether or not VHL Enterprises and Wes World-wide Education Service, Ltd. are non-resident corporations;

3. Whether or not income payments to VHL Enterprises and Wes World-wide Education Service, Ltd are subject to expanded withholding tax.

Considering that the resolution of the first and third issues would depend on the discussion and resolution of the second issue, we deem it necessary and imperative to tackle the second issue first.

Petitioner argues that it had erroneously withheld from VHL Enterprises and WES World-wide Education Service Ltd. final withholding taxes in the total amount of P20,088,435.78 for December 1999 and for the various months of calendar year ending

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December 2000, and remitted the said amounts to the Bureau of Internal Revenue based on its allegedly inaccurate interpretation that VHL Enterprises and WES World-wide Education, Ltd. are non-resident foreign corporations. Accordingly, petitioner withheld and remitted the final withholding tax on its income payments to these foreign corporations based on the corporate tax rates as provided for under the Tax Code, more particularly, at the rates of 33% for the period December 1999 and 32% for the various months of calendar year ended December 2000.

Petitioner rationalizes that VHL Enterprises, with head office in Alabama, U.S.A., and WES World-wide Education Service, Ltd, with head office in England, having rendered hands-on training, instructional and/or consultancy services to the employees of petitioner, and teaching services to the children of the expatriates employed by petitioner, respectively, for a period of almost two years, resulted in their categorization as having set up a "permanent establishment" here in the Philippines. Therefore, petitioner submits that certain pertinent provisions of the RP-US and RP-UK Tax Treaties concerning "business profits" and "permanent establishments", in conjunction with the local tax laws, should be applied in the case at bar. Petitioner cites Articles 4, 5 & 8 of the Republic of the Philippines-United States of America (RP-US) Tax Treaty and Articles 5 & 7 of the Republic of the Philippines-United Kingdom of Great Britain (RP-UK) Tax Treaty, as its bases for the claim. Accordingly, both foreign corporations are rightfully classified as "resident foreign corporations" subject to the five percent (5%) expanded withholding tax under Section 2.57.2 of Revenue Regulations No. 2-98. Pertinent provisions are quoted below for easy reference:

***"RP-US TAX TREATY***

**Article 4. Source of Income.** For purposes of this Convention:

xxx xxx xxx

(6) Notwithstanding paragraphs (1) through (4) business profits which are attributable to a permanent establishment which the recipient, a resident of one of the Contracting States, has in the other Contracting State shall be treated as income from sources within that other Contracting State.

xxx xxx xxx

**Article 8. Business Profits**

(1) Business profits of a resident of one of the Contracting States shall be taxable only in that State unless the resident has a permanent establishment in the other Contracting State. If the resident has a permanent establishment in that other Contracting State, tax may be imposed by that other Contracting State on the business profits of the resident but only on so much of them as are attributable to the permanent establishment.

xxx xxx xxx

(6) The term "business profits" means income derived from any trade or business whether carried on by an individual, corporation or any other person, group of persons, including the rental of tangible personal (movable) property."

**Article 5: Permanent Establishment**

(1) xxx
(2) The term "fixed place of business" includes but not limited to:
a. A seat of management;

b. A branch;
c. An office;
d. A store or other sales outlet;
e. A factory;
f. A workshop;
g. A warehouse;
h. A mine, quarry, or other place of extraction of natural resources;
i. A building site or construction or assembly project or supervisory activities in connection therewith, provided such site, project or activity continues for a period of more than 183 days; and
j. <u>The furnishing of services, including consultancy services, by a resident of one of the Contracting States through employees or other personnel, provided activities of that nature continues (for the same or a connected project) within the other Contracting State for a period or periods aggregating more than 183 days."</u>

***<u>RP-UK TAX TREATY</u>***

**Article 7. Business Profits**

(1) The profits of an enterprise of a Contracting State shall be <u>taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein</u>. If the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in the other State but only so much of them as is directly or indirectly attributable to that permanent establishment.

**Article 5. Permanent Establishment**

xxx xxx xxx

(3) An enterprise of a Contracting State shall likewise be deemed to have a permanent establishment in the other Contracting State if:

a. it carries on supervisory activities within that other Contracting State for more than 183 days in connection with a building site, or a construction or assembly project which is being undertaken, in that other Contracting State; or

b. it furnishes services, including consultancy services, in that other Contracting State through its employees or other personnel (other than agents of an independent status within the meaning of paragraph (7) of this Article) for a period exceeding in the aggregate 183 days within any twelve-month period."

***REVENUE REGULATIONS NO. 2-98***

**Section 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. xxx
B. Professional fees, talent fees, etc. for service of taxable juridical persons – On the gross professional, promotional and talent fees, or any other remuneration enumerated in the preceding subparagraph for the services of taxable juridical persons – five percent (5%)

xxx xxx xxx

Moreover, petitioner asserts that pursuant to Section 3(d) of R.A. 7042, (Foreign Investments Act of 1991) both foreign corporations are considered as "doing business" here in the Philippines. Said Section 3(d) of R.A. 7042 defines "doing business" in this wise:

"(f) The phrase "doing business" shall include soliciting orders, service contracts, opening offices, whether called "liaison" offices or branches; appointing representatives or distributors domiciled in the Philippines or

> who in any calendar year stay in the country for a period or periods totaling one hundred eighty (180) days or more; participating in the management, supervision or control of any domestic business, firm, entity or corporation in the Philippines; and any other act or acts that imply a continuity of commercial dealings or arrangements, and contemplate 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, commercial gain or of the purpose and object of the business organization; xxx."

To bolster this claim, petitioner presented various invoices *(Exhibits II-1 to II-14)*, project time sheets *(JJ-1 to 66)*, proofs of payment of said invoices *(Exhibits KK-1 to KK-14)* and a summary of time sheets issued by VHL Enterprises covering the said services allegedly rendered *(Exhibit JJ)*. For WES World-wide Education Service, Ltd., petitioner presented an invoice *(Exhibit II-15)* and payment thereof *(Exhibit KK-15)*.

We are not convinced.

In the most durable case of **The Mentholatum Co., Inc., et al vs Mangiliman et al, 72 Phil 524**, the Honorable Supreme Court discoursed on the true test to determine whether a foreign corporation is "doing or transacting business" in the Philippines in this manner:

> " 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**." (Emphasis ours)

It is worth emphasizing then that before a foreign corporation may be regarded as doing business here in the Philippines, it is essential to prove that there is the

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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 corporations. Mere allegations by petitioner that the foreign corporations, VHL Enterprises and WES World-wide Education Service, Ltd., have rendered hands-on training services and teaching services, respectively, simply cannot be accepted. The very nature of the corporation and its intention to establish its business continually here in the Philippines has to be satisfactorily proven and convincingly established.

The evidence offered by petitioner to support its claim included, among others, the invoices allegedly issued by VHL Enterprises and WES World-wide Education Service Ltd. and the time sheets issued by petitioner allegedly for the employees of VHL Enterprises who had rendered the said services. According to petitioner, the said invoices and time sheets palpably show the nature and duration of the services rendered by the two foreign corporations here in the Philippines, aggregating more than 183 days for each company.

We strongly disagree.

Given the facts of the case, we cannot see how VHL Enterprises and WES World-wide Education Service, Ltd.'s business dealings with petitioner fit the category of "doing business", considering that it has not been clearly established by petitioner that the transaction or series of transactions were in the nature and character of the business of the foreign corporations. In fact, the nature and character of the business of the two foreign corporations have not even been alleged by petitioner. Petitioner, likewise, failed to prove that the two foreign corporations, VHL Enterprises and WES World-wide Education Service, Ltd., have organized or created an office or place of business, or otherwise put up an agency to conduct their respective trade or business here in the Philippines, so as to be rightfully classified as resident foreign corporations. Both the RP-US and RP-UK Treaties, more specifically under Article 5 (2)(j) and Article 5 (2)(b), respectively, have enumerated those situations wherein a "permanent establishment" may be established, and this court is fairly convinced that nothing in the records presented would reveal and confirm the allegation that the two said foreign corporations have indeed established a "permanent establishment" here in the Philippines.

Additionally, petitioner also failed to show evidence that there was an agreement or a contract between them and the foreign corporations for the alleged services to be rendered. Nor did petitioner present any evidence to prove that both the VHL Enterprises and WES World-Wide Educational Service Ltd. are registered with the Securities and Exchange Commission and are licensed to do business in the Philippines. If indeed, these two corporations are resident foreign corporations, petitioner could have easily presented their income tax returns for the period involved in this case.

Thus, at the most, these series of transactions may be considered only as isolated transactions. The phrase "isolated transaction" has a definite and fixed meaning, i.e., a transaction or series of transactions set apart from the common business of a foreign enterprise in the sense that there is no intention to engage in a progressive pursuit of the purpose and object of the business organization. Whether a foreign corporation is "doing business" does not necessarily depend upon the frequency of its transactions, but more upon the nature and character of the transactions *(Eriks Pte Ltd. vs CA & Enriquez 267 SCRA 567 [1996]).*

In the case of *Island Power Corporation vs. Commissioner of Internal Revenue, CTA Case No. 5922 (May 17, 2004)*, this court, citing the case of *ABB Power Generation Ltd. vs. Commissioner of Internal Revenue, CTA Case No. 4888 (February 6, 1996)* declared that:

> "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."

In the case at bar, there is no showing that VHL Enterprises and WES World-Wide Education Service, Ltd. continued to do business in the Philippines after the hands-on training, instructional and/or consultancy services were rendered to the employees of the petitioner and the teaching services were rendered to the children of the expatriates, respectively.

It must be noted that the invoices issued by the two foreign corporations, likewise, the time sheets issued by petitioner, indubitably failed to show the nature and duration of the services rendered by the two corporations, in contradiction to what is being alleged by petitioner. The said invoices and time sheets merely showed a nonrepresentational data of events and an equivalent amount. These documents failed to convince this court that there was indeed an agreement or contract between the petitioner and the foreign corporations for the rendering of the alleged services and for what duration. In fact, the invoices did not even describe the specific services rendered or to be rendered. Thus, it cannot be concluded from the invoices alone the nature and duration of the services rendered by the said foreign corporations.

As correctly invoked by the petitioner, Section 3(d) of the Foreign Investments Act of 1991 clearly clarified what constitutes as "doing business" here in the Philippines, that is, there must be continuity or the intention to continue the body of its business here in the Philippines. Consequently, it is important to emphasize at this point that the "one hundred eighty (180) days or more" as classified under the said Section 3(d) of the Foreign Investments Act of 1991 must be read in its entirety. It is clear that the phrase "who in any calendar year stay in the country for a period or periods totaling one hundred eighty (180) days" is in connection with the "appointing of representatives or distributors domiciled here in the Philippines". Meaning, the appointed representatives or distributors may be domiciled here in the Philippines, or if not, such appointed representatives or distributors have, in any calendar year, stayed here in the Philippines for one hundred eighty (180) days or more.

In any case, by the mere invoices presented, it is inconceivable to conclude that the foreign corporations' agents have indeed rendered the alleged services for a period of more than 180 days. As has been pointed out by this court, these invoices merely showed a rough outline of events and amounts which do not in any way exemplify nor establish the nature and duration of the services rendered. In fact, not even was there any proof to confirm that there was indeed a contract between the parties. Even the types of services to be rendered by the two foreign corporations were not clearly and convincingly established so as to justify the claim of  petitioner.

Inasmuch as petitioner failed to show that the two foreign corporations are resident foreign corporations, it is fairly concluded that VHL Enterprises and WES World-wide Education Service, Ltd. are nonresident foreign corporations. It follows that they are subject to the final withholding tax as provided for under Section 28(b) of the Tax Code. Accordingly, there was no erroneous payment of final taxes amounting to P22,088,435.78 made to the Bureau of Internal Revenue.

**WHEREFORE**, based on the foregoing discussions, the subject Petition for Review is hereby **DISMISSED** for lack of merit.

**ERNESTO D. ACOSTA**
Presiding Justice

WE CONCUR:

**JUANITO C. CASTAÑEDA, JR.**
Associate Justice

**LOVELL R. BAUTISTA**
Associate Justice

## CERTIFICATION

I hereby certify that the above decision was reached after due consultation with the members of the Court of Tax Appeals in accordance with Section 13, Article VIII of the Constitution.

**ERNESTO D. ACOSTA**
Presiding Justice

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