REPUBLIC OF THE PHILIPPINES
Court Of Tax Appeals
QUEZON CITY

SECOND DIVISION

ENGTEK PHILIPPINES, INC.,
Petitioner,

- versus -

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

CTA CASE NO. 6644

Members:

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

Promulgated:

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D E C I S I O N

PALANCA-ENRIQUEZ, J.:

Is Engtek Philippines, Inc. (hereafter petitioner) entitled to a refund or tax credit for the amount of ₱7,500,000.00, representing payment of income tax on the declared cash dividends alleged to have been erroneously paid?

THE CASE

This issue is before Us in this Petition for Review. Petitioner seeks for a refund of the amount of Seven Million Five Hundred Thousand Pesos (₱7,500,000.00), or in the alternative, for the issuance of tax credit certificate for said amount, representing income tax erroneously paid on April 10, 2001 to respondent.

(187)

THE FACTS

Petitioner, a domestic corporation duly registered and organized under Philippine laws, is engaged in the manufacturing and marketing of electronics and mechanical machinery products, parts and accessories. It is 99.99% owned by Eng Teknologi Holdings Bhd (hereafter "ETHB"), a corporation duly registered and existing under the laws of Malaysia.

On March 7, 2002, petitioner filed an administrative claim for tax credit with Revenue District No. 56 of Calamba, Laguna, in the amount of ₱7,500,000.00, representing withholding tax on the cash dividends to be paid in favor of ETHB. This claim for refund is anchored on the proposition that petitioner resolved to reverse said cash dividend declaration on October 8, 2001 for reasons pertaining to the financial structure of the Eng Tek Group of Companies (to which the petitioner belongs), which at that time had not yet remitted any such dividends to its parent company.

The petition states that petitioner requested the Bureau of Internal Revenue (hereafter "BIR") to offset the withheld amount of ₱7,500,000.00 with taxes that may become due on future declaration of cash dividends. The BIR denied the request on the ground that taxes paid could not be offset with future liabilities.

The claim for tax refund filed with the BIR not having been acted upon, the petitioner elevated its claim to this Court via the present Petition for Review.

185

The Commissioner of Internal Revenue (hereafter respondent), in his answer, alleged, by way of special and affirmative defenses:

> "4. Settled is the rule that tax exemptions cannot be created by implications as they are highly disfavored in law. And considering further that a claim for tax refund partakes of the nature of an exemption, it cannot be allowed unless granted in the most explicit and categorical language (BIR Ruling No. 126-86 dated July 23, 1986).
>
> 5. In an action for refund/credit, 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.
>
> 6. Petitioner has failed to establish any clear interest in or right over the alleged erroneous income tax payment on April 10, 2001.
>
> 7. Petitioner must 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."

Petitioner presented Ma. Portia E. Rosell and Lyn Legaspi, as witnesses, and submitted documentary evidence, marked as Exhibits "A", "B", "C", "D", "E", "G", "H", "L", "N", and "O", together with their submarkings.

On the other hand, respondent submitted the case for decision without presenting any evidence.

Thereafter, both parties were ordered to file their respective memoranda within thirty (30) days from notice. Both parties having complied thereto, the case was deemed submitted for decision. pve

186

THE ISSUES

As stipulated upon by the parties, the following are the issues for this Court's consideration:

I

Whether or not petitioner has complied with the provisions of Sections 204 (C) and 229 of the Tax Code on the prescriptive period for filing administrative and judicial claims for the issuance of tax refund or tax credit certificate.

II

Whether or not petitioner declared cash dividends in the amount of Fifty Million Pesos (₱50,000,000.00) on 20 December 2000.

III

Whether or not Eng Teknologi Holdings BHD is a stockholder of the petitioner which owns 99.99% of the total capital stock of the petitioner

IV

Whether or not the reversal of the declaration of dividends is valid.

V

Whether or not petitioner actually withheld and remitted to the Bureau of Internal Revenue the amount of Seven Million Five Hundred Thousand pesos (₱7,500,000.00) as income tax due on the declared cash dividends..

VI

Whether or not petitioner is the proper party to claim for refund or tax credit in the instant case.

THE COURT'S RULING

As regards the first issue, the Court finds that the administrative and judicial claims for refund were filed within the statutory period of two (2) years after the payment of the tax. A perusal of the "Monthly Remittance Return of Final Income Taxes Withheld" shows that the tax on dividends in the amount of ₱7,500,000.00 was remitted to the BIR on April 10, 2001 (*Exhibit "B"*). Petitioner, therefore, had up to April 10, 2003 within which to file the administrative and judicial claims for refund, pursuant to *Sections 204 and 229, respectively, of the National Internal Revenue Code of 1997, as amended.* Petitioner filed its administrative claim for refund on September 17, 2002 (*Exhibit "G"*) and the judicial claim for refund on April 8, 2003, both well within the two-year prescriptive period.

As regards the second issue, petitioner presented the Secretary's Certificate dated January 26, 2001, which shows that on December 20, 2000, the Board of Directors of the petitioner declared cash dividends in the amount of ₱50,000.000.00. The Secretary's Certificate (Exhibit "A"), in part, reads:

> "SECRETARY'S CERTIFICATE
>
> xxx xxx xxx
>
> 2. At the meeting of the Board of Directors of the Corporation held on 20 December 2000, the following resolutions were approved:
>
> 'RESOLVED, That the Corporation be, as it is hereby, resolved to declare cash

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188

dividends in the total amount of Fifty Million pesos (P50,000,000.00) payable to all shareholders of record as of 30 November 2000 to be taken from the unrestricted retained earnings of the Corporation as of 30 November 2000.'

3. The foregoing are in accordance with the records of the corporation in my possession.

xxx xxx xxx."

Exhibit "A" was identified and attested in open court by Ma. Portia E. Rosell, petitioner's Assistant Corporate Secretary.

Anent the third issue, a perusal of the General Information sheet filed with the Securities and Exchange Commission shows that Eng Teknologi Holdings BHD owns 74,999,993 shares of stock (*Exhibit "N-2"*). This was testified to and confirmed by petitioner's Assistant Corporate Secretary, Ma. Portia E. Rosell, on direct examination. Thus:

"DIRECT EXAMINATION:

ATTY. FERNANDO

Q. You stated earlier, Atty. Rosell, that the Malaysian company and Eng Teknologi Holdings perhaps owned ninety-nine point ninety-nine percent (99.99%) of the Petitioner, Engtek Philippines, incorporated, can you please show where in this document does it indicate?

ATTY. ROSELL

A. On page two (2) of the General Information Sheet for item indicating subscribed capital is the item indicated Subscribed Capital in the total subscribed is P75 million and on page three on the lower half, thereof, is the list of the stockholders and one of the entries is Eng Teknologi Holdings which stated as having subscribed to 74,999,993

> shares. So, by mathematical computation, sir, Eng Teknologi Holdings owned 99.99% of the total subscribed capital of Engtek Philippines, Incorporated" (*TSN, July 29, 2003, pp. 11-12*)

With respect to the fifth issue, the petitioner presented the Certification dated July 17, 2002, issued by Angel A. Monte de Ramos, Jr., Senior Personal Banker OIC, RCBC-Carmelray Business Center, certifying to the fact that they remitted the amount of ₱7,646,700.00, representing payment of Engtek Philippines, Inc. of its final income tax, to the BIR on April 10, 2001 under BCS No. A00049 (*Exhibit "C"*), and the Bank Validated Transfer Form/Debit Advice dated April 9, 2001 (*Exhibit "D"*), the authenticity of which were never disputed nor controverted by the respondent.

With regard to the merits of this petition, the pivotal issue is whether or not the petitioner was able to prove that there was erroneous remittance of withholding tax made to BIR, and, hence, is entitled to a refund of the income tax it paid to the government.

Petitioner argues for the validity of the reversal of declaration of dividends inasmuch as the same was made by petitioner's Board of Directors in a meeting held on October 8, 2001 and which was within the scope of the Board of Directors' corporate powers.

Petitioner asserts that "for reasons pertaining to the financial structure of the Engtek Group of Companies (to which petitioner belongs), petitioner

190

resolved to reverse said cash dividend declaration, and it has not yet remitted any such dividends to its parent company, ETHB".

Citing *Section 2.57.4 of Revenue Regulations No. 2-98, as amended*, respondent, on the other hand, claims that the tax on dividends accrues upon the declaration of the dividends without the need of actual receipt of the income thereof. The cash dividends having been declared on December 20, 2000, the income on dividends by Eng Teknologi Holdings BHD was already taxable, the date of actual receipt thereof being immaterial.

Respondent finally contends that petitioner presented no other documents to prove the validity of the reversal of the dividends or that the same was made pursuant to the reasonable needs of petitioner's business. What was submitted was only the Corporate Secretary's Certificate dated March 31, 2003 showing the resolution of the Board of Directors on October 8, 2001 approving the resolution reversing the previous declaration of cash dividends.

A dividend is that part or portion of the profits of a corporation set aside, declared and ordered by the directors to be paid ratably to the stockholders on demand or at a fixed time (*Fisher vs. Trinidad, 43 Phil. 480; Nielson and Co., Inc. vs. Lepanto Consolidated Mining Co., 26 SCRA 569*).

It is a payment to the stockholders of a corporation as a return upon their investment. It is a characteristic of a dividend that all stockholders of

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191

the same class share in it in proportion to the respective amounts of stock which they hold (*13 Am. Jur.637-639*).

Parenthetically, *Section 43 of the Corporation Code* provides insofar as pertinent:

> "SEC. 43. Power to declare dividends. - The board of directors of a stock corporation may declare dividends out of the unrestricted retained earnings which shall be payable in cash, in property or in stock to all stockholders on the basis of outstanding stock held by them: *Provided*, That any cash dividends due on delinquent stock shall first be applied to the unpaid balance on the subscription plus costs and expenses, while stock dividends shall be withheld from the delinquent stockholders until his unpaid subscription is fully paid; *Provided, further*, That no stock dividend shall be issued without the approval of stockholders representing not less than two-thirds (2/3) of the outstanding capital stock at a regular or special meeting duly called for the purpose.
>
> xxx xxx xxx."

Pursuant to the aforecited provision, the board of directors of a stock corporation has the power to declare dividends out of the "unrestricted retained earnings" which shall be payable in cash, in property, or in stock to all stockholders on the basis of outstanding stock held by them. A mere majority of the quorum of the board of directors is sufficient to declare cash dividends. The board may declare dividends other than stock without need of stockholders' approval.

Under the law, to justify the declaration of dividends, there must be an actual bonafide surplus profits or earnings over and above all debts and liabilities of the corporation (*Steinberg vs. Velasco, 52 Phil. 953*). A dividend declaration ordinarily requires the concurrence of two things, namely:

> 1) the existence of "unrestricted retained earnings" out of which the dividends may be declared and paid; and
>
> 2) a corporate resolution of the board of directors declaring the corporate policy of paying a portion or all of such earnings to the stockholders.

The retained earnings of a corporation is the difference between the total present value of its assets after deducting losses and liabilities and the amount of its capital stock (*11 Fletcher 1041*). Stated otherwise, the ordinary way of determining whether a corporation has retained earnings or not is to compute the value of all its assets, and deduct therefrom all of its liabilities including legal capital, and thus ascertain whether the balance exceeds the amount of its outstanding shares of capital stock. Thus, the retained earnings will be the balance of the net worth or net assets after deducting the value of the corporation's outstanding capital stock. They refer to the accumulated undistributed earnings or profits realized by a corporation arising from the transaction of its business and the management of its affairs, out of current and prior years. Such earnings or portions thereof are said to be unrestricted, and therefore, available for dividend distribution, if they have not been reserved or set aside by the board of directors for some corporate purpose nor are required by law to be earmarked for some other purpose specified by such law (*The Law on Partnerships and Private Corporations, 1997 Ed., by Hector S. de Leon, p. 318*). *pol*

In the case at bench, record shows that on December 20, 2000, the Board of Directors of petitioner adopted the following Resolution to declare cash dividends, to wit:

> "RESOLVED, That the Corporation be, as it hereby, authorized to declare cash dividends in the total amount of Fifty Million Pesos (₱50,000,000.00) payable to all shareholders of record as of 30 November 2000 to be taken from the unrestricted retained earnings of the Corporation as of 30 November 2000." (*Exhibit "A"*)

The resolution's statement, "xxx to declare cash dividends in the total amount of Fifty Million Pesos (₱50,000,000.00) payable to all shareholders of record as of 30 November 2000 to be taken from the unrestricted retained earnings of the Corporation as of 30 November 2000", clearly shows that petitioner had unrestricted retained earnings as of November 30, 2000, out of which cash dividends maybe declared and paid.

Premised on the foregoing, the only logical conclusion is that there was a valid declaration of cash dividends made by petitioner on December 20, 2000.

Record further shows that the withholding tax was remitted to the BIR on April 10, 2001 (*Exhibits "C" and "D"*).

It follows, of course, that a cash dividend, properly and fairly declared by a solvent corporation possessed of ample undivided profits and surplus, under circumstances that made its declaration entirely competent and proper, cannot be revoked by the subsequent resolution of the Board of Directors of the corporation adopted ten (10) months after the declaration of the cash dividends on the alleged ground that the declaration was inopportune. The Resolution dated October 8, 2001, reversing the declaration of the cash dividends reads:

> "WHEREAS, the Corporation declared cash dividend in favor of its stockholders on 20 December 2000;
>
> WHEREAS, the Corporation found the declaration of dividends to be inopportune;
>
> RESOLVED, That the Corporation be, as it is hereby, authorized to reverse its resolution to declare cash dividends dated 20 December 2000;
>
> RESOLVED FINALLY, That the Corporation's Finance Controller be as he is hereby, authorized to sign, execute and deliver any and all documents necessary to carry into effect the foregoing resolution" (*Exhibit "H"*).

The fact that the petitioner declared cash dividends on December 20, 2000 presupposes, and, in fact, clearly shows that the petitioner had actual bonafide surplus profits or earnings over and above all debts and liabilities of the corporation. As a rule, dividends cannot be declared by a corporation until it has eliminated a deficit resulting from its operations of preceding years. Dividends are, thus, payable only when there are profits earned by the corporation. In other words, when a corporation issues cash dividends, it shows that no deficit exists.

Petitioner's argument that for reasons pertaining to the financial structure of the Eng Tek Group of Companies (to which petitioner belongs), it resolved to reverse said cash dividend declaration, is flawed, and without factual and legal basis.

195

Other than the Corporate Secretary's Certificate dated March 31, 2003, showing the resolution of the Board of Directors on October 8, 2001 to prove that on said date the Board approved the resolution reversing the declaration of cash dividends, no other document was presented by the petitioner to prove the financial structure of Eng Tek Group of Companies, to which the petitioner allegedly belongs. Petitioner did not present its book of accounts, certified balance sheet, profit and loss statements, or other equivalent books, that would prove that it had no unrestricted retained earnings at the time of the declaration of cash dividends on December 20, 2000. The allegation simply remained an allegation and no court of justice will regard it as truth. It is well-settled that in an action for refund, the taxpayer has the burden of proof to establish the right to refund. Failure to sustain the burden is fatal to the claim for refund/credit (*Western Minolco Corp. vs. Commissioner of Internal Revenue, 124 SCRA 131*). Petitioner has failed to discharge this burden of proof.

Since petitioner's claim for the entitlement of tax refund or credit remains unproven and unsubstantiated, the same cannot be granted. It is axiomatic in the law of taxation that taxes are the lifeblood of the nation. Hence, "exemptions therefrom are highly disfavored in law and he who claims tax exemption must be able to justify his claim or right" (*Afisco Insurance Corporation vs. Court of Appeals, 302 SCRA 16*).

WHEREFORE, premises considered, the present Petition for Review is hereby **DISMISSED** for lack of merit.

No pronouncement as to costs.

SO ORDERED.

OLGA PALANCA-ENRIQUEZ
Associate Justice

WE CONCUR:

JUANITO C. CASTAÑEDA, JR.
Associate Justice

ERLINDA P. UY
Associate Justice

C E R T I F I C A T I O N

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

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

197