REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

PROCTER & GAMBLE PHILIPPINE
MANUFACTURING CORPORATION,
Petitioner,

- versus -

C.T.A. CASE NO. 2883

THE COMMISSIONER OF INTERNAL
REVENUE,
Respondent.

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1/31/89

D E C I S I O N

This is an action to enforce a claim for a refund or tax credit of an amount of ₱4,832,989.00 representing an alleged overpaid withholding tax on dividends petitioner remitted to its parent company, Procter & Gamble Co., U.S.A.

On April 1 and November 20, 1975, petitioner domestic corporation, a wholly owned subsidiary of Procter & Gamble Co., U.S.A., declared and remitted to the latter, dividends amounting to ₱17,707,460.65 and ₱6,457,485.65, respectively, or a total of ₱24,164,946.30, on which petitioner withheld and paid to the government the amounts of ₱6,197,611.23 and ₱2,260,119.98 or a total of ₱8,457,731.21 as 35% withholding tax. Petitioner, however, claims that pursuant to Section 24(b)(1) of the National Internal Revenue Code, as amended by Presidential Decree No. 369, taken in relation with the provision of Section 902 of the U.S. Internal Revenue

Code, the rates applicable for the dividend remittances should only be 15% instead of 35%. As thus an overpayment of an amount of ₱4,832,989.00 (20% of ₱24,164,946.30), now sought in a claim for a refund or tax credit dated January 5, 1977 which has remained unacted by the respondent Commissioner of Internal Revenue. Hence, the present petition filed on July 13, 1977.

Section 24(b)(1) of the National Internal Revenue Code, as amended by P.D. 369, which allows a preferential tax of 15% on dividends received from a domestic corporation by a non-resident foreign corporation, provides in pertinent part:

> "x x x on dividends received from a domestic corporation liable to tax under this chapter the tax shall be <u>15% of the</u> dividends received, which shall be collected and paid as provided in Section 53(d) of this Code <u>subject to the condition that the country in which the non-resident 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 20%</u> which represents the difference between the regular tax (35%) on corporations and the tax (15%) on dividends as provided in this section. x x x"(Emphasis supplied)

Section 902 of the U.S. Internal Revenue Code, as amended by Public Law 87-834, the law governing tax credits granted to U.S. corporations on dividends received from foreign corporations to the extent applicable reads:

"SECTION 902. <u>CREDIT FOR CORPORATE STOCKHOLDER IN FOREIGN CORPORATION</u>

(a) <u>Treatment of Taxes Paid by Foreign Corporation</u>.- For purposes of this subject, a domestic corporation which owns at least 10 percent of the voting stock of a foreign corporation from which it receives dividends in any taxable year shall -

(1) to the extent such dividends are paid by such foreign corporation out of accumulated profits /as defined in subsection (c)(1)(A)/ of a year for which such foreign corporation is <u>not a less developed country</u> corporation, be deemed to have paid the same proportion of any income, war profits, or excess profits taxes paid or deemed to be paid by such foreign corporation to any foreign country or to any possession of the United States on or with respect to such accumulated profits, which the amount of such dividends (determined without regard to Section 78) bears to the amount of such accumulated profits in excess of such income, war profits, and excess profits taxes (other than those deemed paid); and

(2) to the extent such dividends are paid by such foreign corporation out of accumulated profits /as defined in subsection (c)(1)(B)/ of a year for which such foreign corporation is a <u>less-developed country corporation</u>, be deemed to have paid the same proportion of any income, war profits, or excess profits taxes paid or deemed to be paid by such foreign corporation to any foreign country or to any possession of the United States on or with respect to such accumulated profits, which the amount of such dividends bears to the amount of such accumulated profits.

xxx xxx xxx

(c) Applicable Rules

(1) Accumulated profits defined.- For purposes of this section, the term 'accumulated profits' means with respect to any foreign corporation -

> (A) for purposes of subsections (a)(1) and (b)(1), the amount of its gains, profits, or income computed without reduction by the amount of the income, war profits, and excess profits taxes imposed on or with respect to such profits or income by any foreign country. x x x; and
>
> (B) for purposes of subsections (a)(2) and (b)(2), the amount of its gains, profits, or income in excess of the income, war profits, and excess profits taxes imposed on or with respect to such profits or income.
>
> The Secretary or his delegate shall have full power to determine from the accumulated profits of what year or years such dividends were paid, treating dividends paid in the first 60 days of any year as having been paid from the accumulated profits of the preceding year or years (unless to his satisfaction shows otherwise), and in other respects treating dividends as having been paid from the most recently accumulated gains, profits, or earnings.
>
> xxx xxx xxx."

Petitioner contends that under Section 902 of the U.S. Internal Revenue Code, <u>supra</u>, its parent corporation is allowed to a tax credit equivalent to at least 20% of taxes deemed paid in the Philippines on dividends received as thus illustrated in tactile details:

> The U.S. "deemed paid" tax credit allowed petitioner's parent company on dividends paid to it by petitioner in a year in which it is <u>not a less developed corporation</u> can be determined by the following formula:

Phil. income tax paid on accumulated profits (gains, profits, income without reduction by Phil. income tax)	X	<u>Dividends</u> Accumulated profits in excess of Phil. income tax	=	U.S. deemed paid credit (Foreign tax under Sec. 902(a)(1) of the U.S. Int. Rev. Code

The formula for computing the U.S. "deemed paid" tax credit allowed Procter & Gamble Company on dividends paid to it by petitioner out of accumulated profits in a year in which petitioner is a <u>less developed country corporation</u> is as follows:

Phil. income tax paid on accumulated profits (gains, profits, income in excess of Phil. income tax	X	<u>Dividends</u> Accumulated profits	=	U.S. deemed paid tax credit (foreign tax credit under Sec. 902(a)(2) of the U.S. Internal Revenue Code)

To arrive at the Philippine Income Tax paid on accumulated profits (gains, profits, income in <u>excess</u> of Philippine Income Tax), we compute:

Philippine Income tax	X	Accumulated profits (gains, profits, income <u>less Phil</u>. income tax) gains, profits, income	=	Phil. income tax paid on accumulated profits (gains, profits, income in excess of Phil. Income Tax)

In the second quarter of the calendar year 1975, petitioner declared and remitted in favor of its parent company in the United States dividends amounting to ₱17,707,460.65 on which it paid withholding tax in the amount of ₱6,197,611.23.

Pursuant to Section 902(a) of U.S. Internal Revenue Code, <u>supra</u>, these dividends are deemed to have been paid out of petitioner's most recently accumulated profits, namely, its profits for the fiscal year ended June 30, 1974. For the said fiscal year, petitioner had taxable net income of ₱56,500,332 on which it paid income tax amounting to ₱19,765,116.

If petitioner is not considered a less-developed corporation for its fiscal year ended June 30, 1974, the tax credit allowed Procter & Gamble Company, its parent company, in the United States amounts to ₱9,527,370.52 arrived at as follows:

Gains, profits, and income of petitioner . .	₱56,500,352.00
Philippine Income Tax imposed on or with respect to gains, profits, and income (Total Philippine Income Tax)	19,765,116,00
Accumulated profits (gains, profits, and income without reduction by Philippine Income Tax	56,500,352.00
Dividends paid to U.S. parent company . . .	17,707,460.65
Accumulated profits in excess of Philippine Income Tax (₱56,500,332 less ₱19,765,116)	36,735,216.00

Philippine Income Tax paid on accumulated profits	X	Dividends / Accumulated profits in excess of Philippine income tax	=	U.S. deemed paid tax credit (foreign tax credit under Sec. 902(a)(1) of U.S. Internal Revenue Code)
₱19,765,116	X	₱17,707,460.65 / 36,735,216	=	₱9,527,370.52

The U.S. "deemed paid" tax credit of ₱9,527,370.52 is clearly more than 20% of the dividends remitted by petitioner to its parent company amounting to ₱17,707,460.65. As a matter of fact, it amounts to almost 54% of such dividends. Obviously, the 20% requirement under Section 24(b)(1) of the Tax Code is complied with.

On the other hand, the U.S. tax credit allowed the parent company if petitioner is deemed a less-developed country corporation for its fiscal year ended June 30, 1974 amounts to ₱6,194,478.21, computed as follows:

Gains, profits, and income of petitioner . .	₱56,500,322.00
Philippine Income Tax imposed on or with respect to gains, profits, and income (Total Philippine Income Tax) . . .	19,765,116.00

Dividends paid to U.S. parent company . . ₱17,707,460.65

Philippine Income Tax	X	Accumulated profits / Gains, profits, and income	=	Philippine Income Tax Paid on accumulated profits
₱19,765,116	X	36,735,216 / 56,500,322	=	₱12,850,825.97

Philippine Income Tax Paid on Accumulated profits	X	Dividends / Accumulated Profits	=	U.S. deemed paid tax credit (Foreign tax credit under Sec. 902(a)(2) of the U.S. Internal Revenue Code)
₱12,850,825.97	X	₱17,707,460.65 / 16,735,216	=	₱6,194,478.21

The amount of ₱6,194,478 is about 35% of the dividends amounting to ₱17,707,460.65 remitted by petitioner to its parent company. Hence, the U.S. "deemed paid" tax credit is equivalent to at least 20% of the taxes deemed paid on such dividends in the Philippines.

The dividends declared and remitted by petitioner in favor of its parent company in the second quarter of the calendar year 1975 amounted to ₱17,707,460.65 on which petitioner withheld taxes at the rate of 35% in the sum of ₱6,197,611.23. Twenty (20%) of such dividend which represents the difference between the 35% tax paid (₱6,197,611.23) and the preferential rate of 15% (₱2,656,119.10) amounts to ₱3,541.492.13.

On the other hand, petitioner's parent company is entitled to "deemed paid" tax credit in the United States of ₱9,527,370.52 or about 54% of such dividends if petitioner is not considered a less-developed country corporation , or a tax credit of ₱6,194,478.21 or about 35% of such dividends if petitioner is a less-developed country corporation for its fiscal year ended June 30, 1974.

Clearly, the United States allows petitioner's parent company a tax credit or more than 20% of taxes deemed paid in the Philippines on such dividends. Thus, the preferential 15% tax rate should be the applicable Philippine tax on such dividends.

In the fourth quarter of the calendar year 1975, petitioner declared and remitted in fabor of its parent company in the United States dividends amounting to ₱6,457,485.65 on which it paid withholding tax in the amount of ₱2,260,119.98. These dividends are deemed to have been paid out of petitioner's most recently accumulated profits, namely, its profits for the fiscal year ended June 30, 1975 (See Section 902(c) of U.S. Internal Revenue Code, supra.) For the said year, petitioner had a taxable net income of ₱8,738,125 on which it paid ₱2,952,159 (actually ₱2,988,001 but ₱35,842 was refundable/creditable as overpayment).

If petitioner is not a less developed country corporation for its fiscal year ended June 30, 1975, the tax credit allowed Procter & Gamble, its parent company, in the United States amounts to ₱3,294,786.80, arrived at as follows:

Gains, profits, and income of petitioner ..	₱8,738,125
Philippine Income Tax imposed on or with respect to gains, profits, and income (Total Phil. Income Tax)	2,952,153
Accumulated profits (Gains, profits, and income without reduction by Philippine Income Tax)	8,738,125
Accumulated profits in excess of Philippine Income Tax (₱2,738,125 - ₱2,952,159)	5,785,966
Dividends paid to U.S. parent company ...	6,457,485.65

PHILIPPINE INCOME TAX PAID ON ACCUMULATED PROFITS	X	DIVIDENDS / ACCUMULATED PROFITS IN EXCESS OF PHILIPPINE INCOME TAX	=	U.S. DEEMED PAID TAX CREDIT (Foreign tax credit under Section 902 (a)(2) of the U.S. Int. Revenue Code)
₱2,952,159	X	₱6,457,485.65 / 5,785,966	=	₱3,294,786.80

Obviously, the U.S. "deemed paid" tax credit of ₱3,294,786.80 is more than ₱1,291,497.13 or 20% of the dividends amounting to ₱6,457,485.65 remitted by petitioner to its parent company in the United States. As a matter of fact, it amounts to about 51% of such dividends. Hence, the 20% requirement under Section 24(b)(1) of the Tax Code is thus easily met.

On the other hand, the U.S. tax credit allowed the parent company if petitioner is deemed a less-developed country corporation for its fiscal year ended June 30, 1975 amounts to ₱1,954,777.67, computed as follows:

Gains, profits, and income of petitioner ..₱8,738,125

Philippine Income Tax imposed on or with respect to gains, profits, and income (Total Philippine Income Tax) 2,952,159

Accumulated profits (Gains, profits, and income <u>in excess</u> of Philippine Income Tax) 5,785,966

Dividends paid to U.S. parent company 6,457,485.65

PHILIPPINE INCOME TAX	X	ACCUMULATED PROFITS / GAINS, PROFITS, AND INCOME	=	PHILIPPINE INCOME TAX PAID ON ACCUMULATED PROFITS
₱2,952,159	X	₱5,785,966 / 8,738,125	=	₱1,954,777.67

PHILIPPINE INCOME TAX PAID ON ACCUMULATED PROFITS	X	ACCUMULATED PROFITS / GAINS, PROFITS, AND INCOME	=	U.S. DEEMED PAID TAX CREDIT (Foreign tax credit under Sec. 902(a)(2) of the U.S. Internal Rev. Code)
₱1,954,777.67	X	₱6,457,486.65 / 5,785,966	=	₱2,181,649.31

The amount of ₱2,181,649.31 is about 34% of the dividends amounting to ₱6,457,495.65 remitted by petitioner in favor of its U.S. parent company. Clearly, the U.S. "deemed paid" tax credit is more than 20% of the taxes deemed paid in the Philippines on such dividends.

Petitioner declared and remitted to its parent company in the fourth quarter of the calendar year 1975 dividends amounting to ₱6,457,485.65 on which petitioner withheld taxes at the rate of 35% in

> the amount of ₱2,260,119.98. Twenty per cent (20%) of such dividends, which represents the difference between the 35% tax paid (₱2,260,119.98) and the preferential rate of 15% (₱968,622.85) amounts to ₱1,291,497.13.
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> Petitioner's parent company is allowed a "deemed paid" tax credit in the United States of ₱3,294,786.80 or about 51% of such dividends if petitioner is not a less developed country corporation for its fiscal year ended June 30, 1975, or a tax credit of ₱1,954,777.67 or about 34% of such dividends if petitioner is considered a less-developed country corporation in the said year.
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> Obviously, the United States allows petitioner's parent company a tax credit of more than 20% of taxes deemed paid in the Philippines on such dividends. Hence, the Philippine withholding tax rate imposable is 15%, not 35%.

Respondent avers that the petitioner failed to meet certain conditions necessary in order that the dividends received by the nonresident parent company in the United States be subject to the preferential 15% tax instead of 35%, thus -

> Under U.S. law, the amount of foreign tax paid for which the U.S. taxpayer Procter & Gamble, U.S.A. is entitled to credit, depends upon the proportion which the amount of dividends received bears to the accumulated profits of Procter & Gamble, Philippines with respect to which tax was paid. The privilege of tax credit is not automatically available because only a proportionate part of the income tax paid by Procter & Gamble Philippines to the Philippine Government is credited against the income tax due to the United States government upon dividends received from Procter & Gamble Philippines.
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> In other words, the foreign tax creditable under U.S. law should be at least 20% of the taxes deemed paid in the Philippines following this formula, assuming that the Philippines is categorized a less developed country:

$$\text{Philippine Income Tax} \times \frac{\text{Dividends}}{\text{Accumulated Profits}} = \text{Tax Creditable}$$

> Consequently, petitioner should prove: 1) The Philippine Income Tax; 2) Dividends paid to Procter & Gamble U.S.A.; 3) Accumulated profits as of the end of fiscal years ending 30 June 1974 and 1975; 4) The amount actually credited against the income tax due in the U.S.
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> Petitioner, however, adduced evidence only with respect to the Philippine income tax payments and dividend payments made. No evidence was presented to show the actual amount credited by the U.S. government against the income tax due Procter & Gamble, U.S.A. Neither did petitioner prove the accumulated profits as of the end of fiscal years 1974 and 1975. Petitioner did not collate the accumulated profits but projected on the net income for the fiscal year ended June 30, 1974 in the amount of ₱56,500,332.00 as divisor in ascertaining the U.S. deemed paid tax credit.

And further, that the refund sought would negate the intendment of PD No. 369 because the amount of ₱4,832,989.00 or its equivalent in dollar will be declared as income of the recipient foreign investor and ultimately subjected to income tax by the U.S. government. Hence the U.S. government will benefit from the law supposed to be intended for the foreign investor. And, such is not the philosophy of the Decree to subsidize foreign government through tax sparing system.

The record raises the issue as to whether the petitioner is entitled to the preferential 15% tax rate on dividends declared and remitted to its parent foreign corporation.

It seems to be in place to state that to a certain extent the diverging dialectics in almost every aspect of the exercise are no less different than they might seem, being more of method and emphasis than substance. It might be, and indeed, we think it should be that under Section 902 of the U.S. Internal Revenue Code, supra, petitioner's parent corporation is entitled to a tax credit equivalent to at least 20% of the taxes deemed to have been paid in the Philippines on dividends remitted to it by petitioner. Such being the case petitioner commends itself to this Court that it should be subject to only 15% and not the 35% tax rate on dividends paid to its non-resident parent company in the United States pursuant to Section 24(b)(1) of the Tax Code, supra.

It is urged upon us by the respondent that petitioner failed to show the actual amount credited by the U.S. government against the income tax due Procter & Gamble, U.S.A. on the dividends received. Likewise, petitioner failed to present the income tax return of Procter & Gamble, U.S.A. for 1975 when the dividends were received nor any duly authenticated document showing that the U.S. government credited the 20% tax deemed paid in the Philippines. Let it suffice, however, that Section 24(b)(1) of the Tax Code does not require that an actual tax credit be granted but merely requires that the "country in which the non-resident foreign corporation is domiciled <u>shall allow</u> a credit against the tax due from the non-resident foreign corporation, taxes deemed to have been paid in the Philippines." As aptly noted, the law refers to a"deemed paid" tax credit of 20% which set the quibble at rest.

We likewise find illogic the impression precipitately broached by the respondent that the grant of refund would be violative of the purpose of PD No. 369 since the recipient parent corporation will be taxed by the U.S. government anyway. The records, however, does not show that the U.S. government will tax such refunded amount; but even on the assumption that it will, there is no requirement nor condition in Section 24(b)(1) of the Tax Code that the country of domicile (United States) should not tax the recipient of the dividends on the amount representing the difference between the 35% and 15% preferential tax rate. In adding up to a logical reasoning petitioner puts is upon the simple proposition that, "Moreover, the intention of the law would still be served even if the recipient were taxed on the refund since it would still be benefited to the extent of that portion in excess of the tax paid on the refunded amount. What is important is that the recipient receives a tax benefit since the purpose of the law is to encourage recipient to bring more capital investment." Just so and aptly enough we share such view.

We therefore reach a conclusion no different from the November 15, 1976 ruling of the respondent Commissioner himself conceding to the herein petitioner a preferential rate of a 15% withholding tax at source, quoted in part:

> "Considering that under Sections 901 and 902 of the U.S. Internal Revenue Code, the U.S. parent company will be entitled to a tax credit equivalent to at least 20% of the taxes deemed to have been paid in the Philippines, in addition to the 15% withholding tax, on the said inter-company dividend the conditions provided in the above-cited Section is (sic) fulfilled. (BIR Ruling No. 76-004, July 19, 1976.)
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> "Accordingly, Procter & Gamble Philippine Manufacturing Corporation, as withholding agent, may withhold 15% only on the dividend declared and remitted to its parent company, Procter & Gamble Company, U.S.A."

Far be it from a theoretical gobbledygook the ruling lends settling eloquence to the precise issue in the case at bar. We see no reason for respondent's quick shuttle of a posture by no longer holding the same as his "cup of tea", so to speak. We do not readily uproot a ruling for speculative purpose or simply to gratify idle curiosity.

Accordingly, petitioner is entitled to the sought refund or tax credit of the amount representing the overpaid withholding tax at source and the payment therefor by the respondent hereby ordered. No costs.

SO ORDERED.

Quezon City, Metro Manila, January 31, 1984.

ALEX Z. REYES
Associate Judge

WE CONCUR:

AMANTE FILLER
Presiding Judge

CONSTANTE C. ROAQUIN
Associate Judge