L/B

REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

GENERAL MILLING CORPORATION,
Petitioner,

- versus -

C.T.A. CASE NO. 5173

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:
FEB 19 1997

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# DECISION

Before Us for consideration is a petition for the issuance of tax credit in the aggregate amount of P2,328,257.11 allegedly representing overpaid withholding taxes on royalty and technical assistance fees covering various periods from January 1, 1993 to September 30, 1993.

Petitioner is a domestic corporation organized and existing under and by virtue of Philippine laws. It is principally engaged in the business of manufacturing and marketing flour, milk and other dairy products, yeasts, and other food products.

This petition for review embraces three separate claims for refund which were all originally filed by the petitioner with the Bureau of Internal Revenue (BIR) none of which received any response from said office prompting herein petitioner to consolidate all these claims before this Court on November 15, 1994.

The foremost claim for refund filed by the petitioner with the BIR on September 29, 1993 (Exhibit "A"), embodied in a letter, dated September 28, 1993, pertains to alleged overpaid income tax withheld on royalties remitted to Universal Foods Corporation (UFC), a business entity organized and based in Wisconsin, USA. Petitioner is a licensee of UFC and in consideration of its right to manufacture yeast products through the use of the technology of UFC, it was obliged to pay a royalty fee of 2% of the net sales of the licensed products it was able to manufacture and sell. However, on August 27, 1992, the Licensing and Technical Assistance Agreement between petitioner and UFC was amended reducing the royalty fees from 2% to 1% of the net sales of the licensed products and correspondingly provided for a retroactive application of said reduction starting July 1, 1992. Petitioner alleged that since it had paid withholding tax based on the 2% royalty fees in the total sum of ₱455,206.32 for the period July 1, 1992 to December 31, 1992, there was an overpayment of withholding tax in the sum of ₱227,603.32 on account of the reduction in royalty fees brought about by the amendment, reducing the royalty fees to 1%.

The other claim for refund, dated September 1, 1993 (Exhibit "B"), represents overpayment of withholding tax for the period January 1, 1992 to September, 1992 on royalty and technical assistance fees paid to Campina Melkunie BV United Dairymen (formerly Holland Canned Milk International), a foreign corporation based In Netherlands. Under this licensing agreement, petitioner pays 1% royalty to said corporation for the right to manufacture milk products by availing of the latter's trademarks and technology. Petitioner alleges that it withheld and remitted 35% income tax on the royalty fees it paid to said foreign corporation from the period January 1, 1992 to September 30, 1992 in the total amount of P2,215,949.95.

Meanwhile, the tax treaty between the Philippines and the Netherlands came into force on January 1, 1992. Under Article 12(2)(b) of said treaty, the withholding tax on royalty paid by a Philippine resident to a resident of Netherlands shall not exceed the 15% rate imposed under the Tax Code, as amended. In the light of this provision, petitioner filed on behalf of Campina Melkunie BV, a claim for tax credit of the overpaid withholding taxes it had paid In the amount of P1,266,257.11 with the International Tax Affairs Division of the Bureau of Internal Revenue.

The final claim for refund included in this petition was filed with respondent on November 24, 1993 (Exhibit "C") representing overpayment of withholding tax on royalty payments made to foreign licensors who are residents of the United States in compliance with Revenue Memorandum Circular (RMC) No. 39-92 which in part provides:

> "2. Taxpayers who have relied on such rulings, but are not the recipients of such rulings directly providing for the "most favored nation" tax rate of 10% on their royalty payments, and accordingly have failed to withhold the correct taxes on royalties paid to recipients in the United States are deemed to be deficient in their tax payments beginning from such date that they have started paying the incorrect amount of taxes of 10%. These taxpayers cannot claim that they have a vested right to such "most favored nation" tax treatment which cannot be given retroactive application. As such, these taxpayers are given not later than October 30, 1992 to amend their withholding tax returns and pay the corresponding taxes, without the penalties...."

On July 21, 1993, this Court made the pronouncement in the case of **IBM Philippines, Inc. v. Commissioner of Internal Revenue, CTA Case No. 4308**, that royalty payments made to residents of the United States shall be subject to only 10% withholding tax under the "most favored nation clause" of the R.P. - U.S. Tax Treaty. Petitioner then filed a claim for tax credit for excess withholding taxes it paid under protest in the total amount of P813,610.46, representing the difference in the amount of taxes paid at 35% and the amount of tax that should have been paid which was pegged at only 10% of the royalties remitted to residents of the United States.

The consolidated claims of the petitioner may thus be summed up as follows:

| | | |
|---|---|---|
| claim dated September 28, 1993 - | | P 227,608.32 |
| claim dated September 1, 1993 - | | 1,266,257.11 |
| claim dated November 18, 1993 - | | 813,610.46 |
| | TOTAL | P2,328,257.11 |

In answer to the petition, respondent did not individually tackle each claim of the petitioner but made a general statement that the claim for refund filed by the petitioner had already prescribed and that the amount of P2,328,257.11 sought to be refunded was not properly documented.

For purposes of clarity, we shall discuss each claim for refund separately.

I

The claim, dated September 28, 1993, in the amount of P227,608.32 was premised on the allegation of petitioner that the Licensing and Technical Assistance Agreement it entered into with Universal Foods Corporation (UFC) was amended, resulting in the reduction of royalty fees from 2% to 1% of the net sales of the licensed products. Said amendment also provided for a retroactive application of this reduction starting July

1, 1992. The corresponding decrease in the taxable base resulted in a lower withholding tax rate, thus an overpayment occurred which petitioner asserts to be refundable.

Petitioner was able to prove, among others, the reduction of the royalty fees from 2% to 1% by presenting the "Amended Licensing and Technical Assistance Agreement" which provided that royalty fees shall be lowered from 2% to 1% of the net sales of the licensed products manufactured and sold (Exhibits "A-1" and "A-1-a"). Petitioner also presented the Monthly Remittance Returns of Income Taxes Withheld (BIR Form 1743W) for the period July to December 1992 (Exhibits "A-3" to "A-16") to prove its remittance of the withholding taxes due to the Bureau of Internal Revenue. However, in the face of the evidence presented by the petitioner, this Court is not inclined to grant petitioner's request for tax credit in the amount of P227,603.32. This denial is predicated on its failure to show that the resulting overpaid royalties comprising the excess 1% royalty fees after the reduction and previously remitted to UFC, have been actually repatriated or remitted back to the licensee, herein petitioner.

No evidence whatsoever was presented to establish the return of the excess royalties if indeed the overpaid royalties were given back by UFC to the petitioner.

We cannot simply rely on the amended Licensing and Technical Assistance Agreement offered in evidence by the petitioner. The agreement is only an expression of the will of the parties. Petitioner's right to the claims can be required of the government only after it has proven, without doubt, that it was so reimbursed with the excess 1% royalty fees. Evidence on record, however, does not bear this out. The undisputed fact still remains that petitioner actually paid 2% royalty fees despite the existence of the agreement which, to the mind of this Court, has not been properly demonstrated to have been implemented or consummated by the parties to the agreement.

It is the paramount duty of this Court to guard against the possibility of granting claims based on alleged reduced royalty fees founded on an amended agreement which, in truth, may reveal eventually the fact that no such real reduction ever transpired between the parties. In such a situation, the government will be at the losing end.

II

The claim for refund, dated September 1, 1993, filed by the petitioner in behalf of Campina Melkunie BV in the amount of P1,266,257.11 based on the reduced withholding tax rate on royalty fees dictated by Article 12(2)(b) of the RP-Netherlands Tax Treaty, cannot be given credence as the same is considered to have prescribed in accordance with Section 230 of the Tax Code, which provides as follows:

> **Sec. 230. Recovery of tax erroneously or illegally collected.** - No suit or proceeding shall be maintained in any court for the recovery of any national internal revenue tax hereafter alleged to have been erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority, or of any sum alleged to have been excessive or in any manner wrongfully collected, until a claim for refund or credit has been duly filed with the Commissioner; but such suit or proceeding may be maintained, whether or not such tax, penalty, or sum has been paid under protest or duress.
>
> In any case, no such suit or proceeding shall be begun after the expiration of two years from the date of payment of the tax or penalty regardless of any supervening cause that may arise after payment: **Provided, however**, That the Commissioner may, even without a written claim therefore refund or credit any tax, where on face of the return upon which payment was made, such payment appears clearly to have been erroneously paid.

Withholding taxes on royalties are considered final taxes as provided in Section 50(a) of the Tax Code, thus:

> **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), (a)(6)(C)(ii), (b)(1), (b)(2), (b)(3), (b)(4), (b)(5)(A), (b)(5)(B), (b)(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.

Section 25(b)(1) mentioned in the above-quoted provision refers to taxes on non-resident foreign corporations one of which pertains to withholding taxes on royalties as in the instant case. The Tax Code also provides that the final withholding taxes mentioned in Section 50 shall be paid within 25 days from the close of each calendar quarter as seen from the provision of Section 51(a) quoted hereunder as follows:

> Sec. 51. ***Returns and payment of taxes withheld at source.*** - (a) *Quarterly returns and payment of taxes withheld.* - Taxes deducted and withheld under Section 50 shall be covered by a return and paid to the Revenue District Officer, Collection Agent, or duly authorized treasurer of the city or municipality where the withholding agent has his legal residence or principal place of business, or where the withholding agent is a corporation, where the principal office is located. The taxes deducted and withheld by the withholding agent shall be held as a special fund in trust for the Government until paid to the collecting officers. The Commissioner of Internal Revenue may, with the approval of the Secretary of Finance, require these withholding agents to pay or deposit the taxes deducted or withheld at more frequent intervals when necessary to protect the interest of the Government. The return for

> final withholding tax shall be filed and the payment made within 25 days from the close of each calendar quarter, while the return for creditable withholding taxes shall be filed and the payment made not later than the last day of the month following the close of the quarter during which withholding was made. (as amended by B.P. Blg. 41).

However, Revenue Regulations No. 5-85, particularly Section 2 provided for the synchronization of the time and manner of remitting certain taxes, among which are the final taxes mentioned in Section 50(a) (supra). Section 2 of said Revenue Regulation directs that the final taxes shall be remitted within ten (10) days after the end of each calendar month with the filing of the appropriate returns. Section 2 of Revenue Regulations No. 5-85 is quoted hereunder, thus:

> Sec. 2. - ***Monthly Return and Remittance of Taxes Withheld*** - Taxes deducted and withheld on:
>
> (i) compensation income,
>
> (ii) income payments subject to the creditable (expanded) withholding taxes, and
>
> <u>(iii)income subject to final withholding taxes</u> (underscoring supplied)
>
> shall be remitted within ten (10) days after the end of each calendar month with the filing, of the appropriate returns as follows:
>
> BIR FORM NO. W-1a - For taxes withheld on Compensation Income
>
> BIR FORM NO. 1743-A1 - For Creditable (expanded) withholding taxes

BIR FORM NO. ______ - For final income taxes withheld

In conformance to the aforequoted Revenue Regulation, petitioner herein paid final taxes on the royalties it remitted to UFC covering the period January 1992 to September 1992 on the 10th day after the end of each calendar month. These payments are shown by Exhibit B-20 which contains an itemized list of the payments made by petitioner and the dates when these amounts were paid. Shown hereunder is the list aforementioned:

| Date | Check No. | Amount |
|---|---|---|
| 02-10-92 | 005303 | 5,109,640.71 |
| 03-10-92 | 005683 | 1,970,885.38 |
| 04-10-92 | 006108 | 2,300,885.81 |
| 05-13-92 | 006489 | 3,121,998.06 |
| 06-09-92 | 006976 | 3,263,859.82 |
| 07-09-92 | 007768 | 3,021,509.24 |
| 08-07-92 | 008898 | 4,960,271.33 |
| 09-08-92 | 010078 | 4,874,151.45 |
| 10-09-92 | 010691 | 2,893,119.37 |

Unfortunately, all such claims for refund have all prescribed as correctly pointed out by the respondent. The present petition for review was filed on November 15, 1994 and when reckoned from the last date of payment of the tax for the instant claim for refund which was on October 9, 1992 (see above list), the total period of two (2) years, one (1) month and six (6) days have elapsed, well beyond the two-year prescriptive period provided for in Section 230 of the Tax Code, (supra).

Section 230 of the Tax Code assigns a two-year period within which to institute a claim for refund both in the administrative as well as in the judicial level, and this was clearly explained by the Supreme Court in the case entitled **Commissioner of Internal Revenue v. Victorias Milling Co., Inc., 22 SCRA 12**, when it ruled:

> "We have repeatedly held that the claim for refund with the Bureau of Internal Revenue and the subsequent appeal to the Court of Tax Appeals must be filed within the two-year period. If however, the Collector takes time in deciding the claim and the period of two years is about to end, the suit or proceeding must be started in the Court of Tax Appeals before the end of the two-year period without awaiting the decision of the Collector."

Thus, in the instant case the claim for refund in the total amount of P1,266,257.11 cannot be granted on the ground of prescription.

III

The last claim for refund in the total amount of P813,610.46 representing overpaid withholding taxes is premised on petitioner's theory that royalties paid to US licensors is subject to only a 10% withholding tax in accordance with this Court's ruling in the case entitled **IBM Philippines, Inc. v. Commissioner of Internal Revenue, CTA Case No. 4308**, dated July 21, 1993. The amount of P813,610.46 represents the alleged excess payments made by the petitioner covering the periods

January 1, 1983 to July 31, 1992 and July 1, 1992 to September 30, 1993, broken down as follows:

| | |
|---|---|
| Excess Withholding Tax payments made for the period Jan. 1, 1983 to July 31, 1992 | ₱678,675.51 |
| Excess Withholding Tax payments made for the period July 1, 1992 to September 30, 1993 | ₱134,934.95 |
| TOTAL | ₱813,610.46 |

A review of the evidence presented by the petitioner leads this Court to conclude that the claims for refund of taxes paid during the period covering January 1, 1983 to October 30, 1992 have already prescribed pursuant to Section 230 of the Tax Code as earlier discussed. It should again be noted that the judicial claim for refund via this petition for review was filed on November 15, 1994 which date is beyond the two-year prescriptive period when reckoned from the dates of payment of the two monthly remittance returns for the month of October, 1992 (Exhibit "C-14") and November 11, 1992 (Exhibits "C-15" and "A-10"). Therefore, the claims for refund pertaining to payments made outside the two-year period, having the date of November 15, 1994 as reference, have all prescribed.

It was also observed by this Court that the payment allegedly made during the month of September, 1993 is not substantiated by the evidence submitted by the petitioner and consequently denied for lack of proof of payment.

As to the rest of the claims that fall within the two-year prescriptive period, this Court finds them with sufficient legal basis and properly supported by the evidence submitted.

In the case entitled **IBM Philippines, Inc. v. Commissioner of Internal Revenue**, CTA Case No. 4308, July 21, 1993, this Court ruled that royalties remitted by a resident of the Philippines to a resident of the United States shall be subject to a reduced withholding tax rate of 10% and not 25% earlier imposed in accordance with Article 12(2)(b) of the R.P.-West Germany Tax Treaty. Portions of said decision are quoted hereunder, thus:

> "This Court is of the persuasion that petitioner's stand is correct and concurs with the opinion rendered by then Commissioner of Internal Revenue, Bienvenido Tan, Jr. (BIR Ruling No. 456-88, supra., that under the most favored nation provision of the R.P.-U.S. Tax Treaty (Article 13, paragraph 2(b)(iii), the tax imposable on royalties derived by a resident of the United States from sources within the Philippines shall be the lowest rate of Philippine tax that may be imposed on royalties of the same kind paid under similar circumstances to a resident of a third, state. Article 12, paragraph 2(b) of the R.P.-West Germany Tax Treaty, provides that royalties arising in the Philippines and paid to a resident of West Germany may also be taxed in the Philippines, but the tax so charged shall not exceed 10% of the gross amount of royalties. Said treaty also provides that for

as long as the transfer of technology under Philippine law, is subject to approval, the limitation of the tax rate in case of royalties arising in the Philippines, apply if the contract giving rise to such royalties has been approved by Philippine competent authorities."

This aforecited ruling was adopted by this Court in similar other cases such as:

1) Abbot Laboratories (Philippines) v. Commissioner of Internal Revenue, CTA Case No. 5119, September 9, 1996;

2) S.C. Johnson and Son, Inc. v. Commissioner of Internal Revenue, CTA Case No. 5136, May 7, 1996;

3) Armco Marsteel Alloy Corporation v. Commissioner of Internal Revenue, CTA Case No. 5115, February 6, 1996; and

4) Gillette (Philippines), Inc. v. Commissioner of Internal Revenue, CTA Case No. 4248, February 8, 1995.

In support of its claim, petitioner has submitted, among others, its application for Relief from Double Taxation (BIR Form No. TC-001), the corresponding Monthly Remittance Returns of Income Taxes Withheld (BIR Form 1743W) and the Technical Assistance Agreement duly approved and registered with the Bureau of Patents, Trademarks and Technology Transfer (Exhibits "C-1", "C-5", "C-16" to "C-35" and "A-1").

In summary, the monthly claims that are to be granted to the petitioner are enumerated hereunder, to wit:

Payments made at 25% withholding tax:

| | Exhibit | Amount | |
|---|---|---|---|
| November 1992 | C-16, 17 | P85,322.78 | |
| December 1992 | C-18, 19 | 99,162.70 | |
| January 1993 | C-21 | 25,054.97 | |
| February 1993 | C-23 | 7,646.69 | |
| March 1993 | C-24, 25 | 40,799.69 | |
| April 1993 | C-26, 27 | 11,410.44 | |
| May 1993 | C-29 | 7,528.47 | |
| June 1993 | C-31 | 4,066.29 | |
| July 1993 | C-33 | 8,451.02 | |
| August 1993 | C-35 | 1,512.42 | |
| Total | | | P290,955.47 |

Less: 10% Withholding tax on Royalties under the "Most Favored Nation Clause":

| | | |
|---|---|---|
| November 1992 | P 341,291.12 | |
| December 1992 | 396,650.78 | |
| January 1993 | 77,119.94 | |
| February 1993 | 105,537.92 | |
| March 1993 | 163,200.77 | |
| April 1993 | 93,335.75 | |
| May 1993 | 49,698.87 | |
| June 1993 | 37,296.17 | |
| July 1993 | 56,695.08 | |
| August 1993 | 29,041.70 | |
| Total | P1,349,868.10 | |
| Multiply by | 10% | 134,986.81 |
| Overpayment/Amount available for tax credit | | P155,968.66 |

**WHEREFORE**, in view of the foregoing premises, only the claim for refund, dated November 18, 1993, referring to overpaid income taxes on royalties remitted to U.S. Licensors is hereby PARTIALLY GRANTED. The two other claims for refund dated September 28, 1993 and September 1, 1993 are both **DENIED** for lack of merit.

**ACCORDINGLY**, respondent is **ORDERED** to **ISSUE** a Tax Credit Certificate in the amount of P155,968.66 in favor of the petitioner.

SO ORDERED.

RAMON O. DE VEYRA
Associate Judge

I CONCUR:

ERNESTO D. ACOSTA
Presiding Judge

## CERTIFICATION

I hereby certify that this 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 Judge
Court of Tax Appeals