REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

HONGKONG - SHANGHAI HOTELS, LTD.,
Petitioner,

- versus -

C.T.A. CASE NO. 5243

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:
APR 29 1999

x - x

DECISION

This case involves a claim for refund of alleged erroneously paid branch profit remittance tax for the years 1991 and 1992 in the total amount of ₱1,828,323.96.

Petitioner is the Philippine branch of a foreign corporation engaged in the business of hotel management. For the years 1991 and 1992, it accumulated branch profits amounting to ₱10,044,896.00 and ₱8,980,834.00, respectively, which it eventually remitted to its Head Office. And so, on April 12, 1993 and February 10, 1994, Petitioner filed its Monthly Remittance Returns of Income Taxes Withheld and paid the amounts of ₱1,310,204.00 and ₱1,171,413.13, respectively, representing the 15% branch profit remittance tax computed on the basis of the 1991 and 1992 profits remited by Petitioner to its Head Office, as follows:

1991

$$\frac{₱10,044,896.00}{1.15} \times 15\% = ₱1,310,203.80$$

1992

$$\frac{₱\ 8,980,834.00}{1.15} \times 15\% = ₱1,171,413.10$$

On the strength of Section 25(a)(5) of the Tax Code which provides:

> (5) Tax on branch profits remittances. - Any profit remitted by a branch to its head office shall be subject to a tax of 15% (except those registered with the Export Processing Zone Authority): Provided, That any profit remitted by a branch to its head office authorized to engage in petroleum operations in the Philippines shall be subject to tax at $7^1/_2$%. In both cases, the tax shall be collected and paid in the same manner as provided in Sections 51 and 52 of this Code: and Provided, further, <u>That interests,</u> dividends, rents, royalties, including remuneration for technical services, salaries, wages, premiums, annuities, emoluments or other fixed or determinable annual, periodical or casual gains, profits, income and capital gains <u>received by a foreign corporation during each taxable year from all sources within the Philippines shall not be considered as branch profits unless the same are effectively connected with the conduct of its trade or business in the Philippines,</u>" (Underscoring supplied)

Petitioner filed on April 10, 1995 an administrative claim for refund (Exh. E) in the amounts of ₱1,082,487.44 for 1991 and ₱745,836.52 for 1992, or a total of ₱1,828,323.96, representing the branch profit remittance tax pertaining to the interest income included as part of the branch profits remitted computed as follows:

A. Branch Profit Remittance Tax Actually Due

1992

Total Profits Remitted	₱ 8,980,834.00
Less: Interest Income	5,718,080.00
BPRT Tax Base	₱ 3,262,754.00
$\frac{3,262,754}{1.15}$ x 15% = BPRT actually due =	₱ 425,576.61

1991

Total Profits Remitted	₱10,044,896.00
Less: Interest Income	8,299,069.00
BPRT Tax Base	₱ 1,745,827.00
$\frac{1,745,827}{1.15}$ x 15% = BPRT actually due =	₱ 227,716.56

B. Branch Profit Remittance Tax Refundable

1992

BPRT Paid	₱ 1,171,413.13
Less: BPRT Actually Due	425,576.61
Refundable BPRT	₱ 745,836.52

1991

BPRT Paid	₱ 1,310,204.00
Less: BPRT Actually Due	227,716.56
Refundable BPRT	₱ 1,082,487.44

As there was no immediate action on the part of herein Respondent, the instant petition was filed on April 12, 1995 to toll the running of the two-year prescriptive period. In his Answer, Respondent claimed by way of Special and Affirmative Defenses that:

> 4. Petitioner's income from all sources within the Philippines is taxable likewise in the Philippines. Corollarily, any remittance

thereon to its parent company is subject to branch profit remittance tax;

5. In view of the fact that the 15% branch profit remittance tax is imposed and collected at source necessarily the tax base in computing the said tax should be the amount actually applied for by the branch (Petitioner) with the Bangko Sentral ng Pilipinas as profit to be remitted abroad. (Revenue Memorandum Circular No. 8-82 dated March 17, 1982; Compania General de Tabacos de Filipinas, Phil. Br. vs. CIR, CTA Case No. 3827, October 14, 1989);

6. Taxes are presumed to have been collected in accordance with law;

7. In an action for refund of taxes, it is incumbent upon the taxpayer to show that the taxes paid were erroneously or illegally collected, failure to sustain the burden is fatal to the action claiming for the refund;

8. Claims for refund of taxes are construed strictly against claimants, the same being in the nature of exemptions from taxation. (Manila Electric Co. vs. CIR, 67 SCRA 351).

The sole issue for determination is whether or not the interest income earned by Petitioner and remitted to its Head Office may properly be treated as Branch Profit subject to the Branch Profit Remittance Tax.

Petitioner alleges that under the aforecited Section 25(a)(5) of the Tax Code, the interest income it derived from bank placements is not effectively connected with its business of hotel management. Hence, the said interest income should not have been included as part of the profits subject to the 15% branch profit remittance tax.

To support its claim, Petitioner submitted the bank deposit advices issued by the Hongkong Shanghai Banking Corporation for the years 1991 and 1992 showing the corresponding amount of interest income earned by Petitioner on its money market placements (Exhs. F-1 to F-1-335 and G-1-177). These advices were allegedly previously verified by SGV & Co., which issued a certification to the effect that based on the procedures performed, only ₱8,109,439.00 out of the reported ₱8,299,069.00 in 1991 and ₱5,684,502.00 out of the ₱5,718,080.00 in 1992 were fully supported by bank deposit advices (Exh. F).

Respondent, on the other hand, presented no controverting evidence and maintained that the issue in this case is purely legal.

We find for the Petitioner.

Section 25(a)(5) of the Tax Code explicitly states that interests received by a foreign corporation during each taxable year from all sources within the Philippines <u>shall not be considered as branch profits</u>. The only exception is when the same are effectively connected with the conduct of its business in the Philippines. Petitioner's case does not fall under the exception. The interest income it derived from bank placements has nothing to do with its business of hotel management.

Accordingly, the same cannot be treated as branch profit subject to the branch profit remittance tax.

Furthermore, this is not the first time that We have been confronted with such an issue. As aptly cited by Petitioner, in **Compania General de Tabacos de Filipinas vs. The Commissioner of Internal Revenue (CTA Case No. 4451, August 23, 1993)**, We ruled:

> "More credible is the stand of petitioner. As worded in Section 24(b)(2)(ii), the rule is interest and dividends received by a foreign corporation during each taxable year from all sources within the Philippines shall not be considered as branch profits unless the same are effectively connected with the conduct of its trade or business. The phrase "effectively connected" was interpreted to mean income derived from the business activity in which the corporation is engaged.
>
> In all the corporate quarterly income tax returns filed by petitioner with respondent's office, it was indicated as it was shown that the petitioner is engaged in the business of leaf tobacco dealer, exporter, importer and general merchants. Petitioner claims that interests received from savings deposit with PhilTrust, interests received from money market placements and interest on and Bank Bonds and cash dividends received from Philippine Long Distance Telephone Company (PLDT) and Tabacalera Industrial Development Corporation of the Phils. are not effectively connected with its trade or business.
>
> Furthermore, pursuant to Section 24(c) and(d) of the NIRC, dividends and interest are subject to final tax. To include them again as subject to branch profit remittance tax under the same Section 24(b)(2)(ii) would be contrary to law. Rightfully so, petitioner has sufficiently established a right to be refunded the amount of branch profit remittance tax paid on these interests and dividends which were

included as part of the branch profits for 1985 (partial) and 1986."

In view, however, of the findings of SGV & Co. noting the absence of some supporting documents, We are reducing Petitioner's claim to ₱1,799,209.88, computed as follows:

A. Branch Profit Remittance Tax Actually Due

1992

Total Profits Remitted	₱ 8,980,834.00
Less: Interest Income	5,684,502.00
BPRT Tax Base	₱ 3,296,332.00
$\frac{3,296,332}{1.15}$ x 15% = BPRT actually due =	₱ 429,956.34

1991

Total Profits Remitted	₱10,044,896.00
Less: Interest Income	8,109,439.00
BPRT Tax Base	₱ 1,935,457.00
$\frac{1,745,827}{1.15}$ x 15% = BPRT actually due =	₱ 252,450.91

B. Branch Profit Remittance Tax Refundable

1992

BPRT Paid	₱ 1,171,413.13
Less: BPRT Actually Due	429,956.34
Refundable BPRT	₱ 741,456.79

1991

BPRT Paid	₱ 1,310,204.00
Less: BPRT Actually Due	252,450.91
Refundable BPRT	₱ 1,057,753.09
Total Amount Refundable	₱ 1,799,209.88

WHEREFORE, in view of the foregoing, Respondent Commissioner of Internal Revenue is hereby **ORDERED** to **REFUND** or, in the alternative, **ISSUE** a TAX CREDIT

CERTIFICATE, to Petitioner, the amount of ₱1,799,209.88 representing erroneously paid branch profit remittance tax for the years 1991 and 1992.

SO ORDERED.

AMANCIO Q. SAGA
Associate Judge

WE CONCUR:

ERNESTO D. ACOSTA
Presiding Judge

RAMON O. DE VEYRA
Associate Judge

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 Judge