REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

STEPAN PHILIPPINES, INC.,
Petitioner,

- versus -

C.T.A. CASE NO. 5695

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:
SEP 01 2000

x - x

DECISION

This is a Petition for Review filed by Petitioner STEPAN PHILIPPINES, INC. against Respondent COMMISSIONER OF INTERNAL REVENUE for failure of the latter to act on the former's claim for refund in the amount of P936,288.01, representing its alleged erroneously paid creditable withholding taxes for the year 1996.

As represented, Petitioner is a domestic corporation with principal address at the 17th Floor, UCPB Building, Makati Avenue, City of Makati. It is registered with the Board of Investments (BOI) as a pioneer enterprise, engaged in the manufacture of coco fatty alcohol sulfactants, pursuant to the provisions of Executive Order No. 226, otherwise known as the Omnibus Investments Code of 1987. It started its commercial operation in July 1997 (p. 70, docket, TSN dated April 23, 1999, p. 40).

In the year 1996, Petitioner's income from sales of its goods produced on the trial run of its operation amounting to P93,628,801.77 were allegedly subjected by Procter and

Gamble Philippines,, Inc., the buyer of said products produced in said test runs, to a 1% creditable withholding tax in the total amount of P936,288.01 (Exh. E, TSN, April 23, 1999, pp. 13 to 16).

On May 22, 1997, Petitioner filed with Respondent its Corporate Annual Income Tax Return (ITR) for the year 1996 (Exh. B). In the said return, Petitioner declared a zero sale and income for the year 1996 on the ground that it had no commercial operation during that year (TSN, April 23, 1999, p. 23), and further declared the amount of P936,288.00, allegedly representing the 1% creditable withholding tax withheld by Procter and Gamble Phils., Inc. on its income payments to Petitioner during the taxable year of 1996, as a refundable amount. It filed its administrative claim for refund with Respondent on April 4, 1997 (Exh. F).

However, the aforesaid amount of P936,288.00 was likewise carried over by Petitioner to the year 1997, as shown in its ITR for the said year, which was filed by Petitioner with Respondent on May 15, 1998 (Exh. C). Petitioner showed a nil tax liability in the said 1997 ITR alleging that it enjoys income tax holiday for six years, pursuant to Article 39 (a)(1) of the Omnibus Investments Code of 1987 (E.O. 226), which provides:

> **Art. 39.** ***Incentives to Registered Enterprises.*** - All registered enterprises shall be granted the following incentives to the extent engaged in a preferred area of investment:
>
> (a) Income Tax Holiday –
>
> (1) For six (6) years from commercial operation for pioneer firms and four (4) years for non-pioneer firms, new registered firms shall be fully exempt from income taxes levied by the National Government. x x x (Underscoring supplied)

The aforesaid administrative claim for refund dated April 4, 1997, was not acted upon by the Respondent, hence, on November 20, 1998 Petitioner filed with this Court the instant Petition for Review.

Petitioner's raison d'etre for its Petition for Review is that under Article 39, par. (a)(1) of Executive Order No. 226, it is a preferred pioneer enterprise and is, therefore, entitled to income tax holiday for a period of six years from the start of its commercial operation starting in July, 1997 as explicitly stated in the Specific Terms and Conditions per BOI Board, Minutes of September 4, 1997 (p. 70 docket, TSN dated April 23, 1999, p. 40) and not in July, 1994 as mentioned in the Letter Request for Issuance of a Certificate of Exemption (TSN, April 23, 1999, pp. 36 to 38). Inasmuch as it only started its commercial operation in July, 1997, Petitioner argued that income payments made to it in 1997 should not be subject to any creditable withholding tax as it is exempt from income tax during that period. Likewise, it said that it was not able to utilize the amount of P936,288.00 representing the 1% creditable withholding tax (CWT) which Procter and Gamble Philippines withheld on its income payments made to it in 1996 in the total amount of P93,628,801.77, alleging that during said year, it had no income to declare precisely because it was not yet in operation (TSN, April 23, 1999, p. 23). Neither was it utilized in the succeeding year of 1997 because it already enjoyed a tax holiday during the said year (TSN, April 23, 1999, p. 25). Hence, the claim for refund.

Respondent, on the other hand, argued that Petitioner is not entitled to the claimed refund on the grounds that the declaration of Petitioner that it had no commercial operation in 1996 is highly irregular and inconsistent with its allegation that the claimed refund of P936,288.00 was withheld from the income payments made to it by Procter and Gamble Philippines. Respondent further alleged that Petitioner failed to meet the requirement provided by jurisprudence in claiming the refund of creditable withholding taxes, when it failed to show in the return of the recipient that the income payment received was declared as part of gross income.

Thus, the sole issue is whether or not the amount of P936,288.00, allegedly representing the 1% CWT withheld by Procter and Gamble Philippines from its income payments to Petitioner in 1996 in the total amount of P93,628,801.77 which was not declared by Petitioner in its ITR in 1996, is refundable.

Prefatorily, it must be stressed that the Court finds no obscurity or ambiguity in the language of Article 39(a)(1) of Executive Order No. 226, *supra,* insofar as the same is brought to bear upon the circumstances of Petitioner in the case at bar. The provision is crystal clear that all enterprises registered with the BOI under the Omnibus Investments Code of 1987 (E.O. 226) are exempt from income taxes (including the creditable withholding taxes) for six (6) years for those with status of a pioneer enterprise, and four (4) years for those with status of a non-pioneer enterprise, from the start of its commercial operation. Thus, a taxpayer falling within the ambit of the aforementioned provision of law, whose income was subjected to creditable withholding tax by its customers/withholding agents, should likewise be entitled to a refund of the same as the creditable withholding taxes are in the nature of an advance payment by the said taxpayer to its income tax liability at the end of the taxable year.

In the case at bar, Petitioner has clearly established that it falls within the mantle of Article 39 (a)(1) of E.O. 226 and that it started its commercial operation in July, 1997, therefore, no other conclusion can be drawn that Petitioner's income in 1997 is exempt from income taxes under the National Internal Revenue Code (NIRC), including withholding taxes.

However, with regard to Petitioner's creditable withholding taxes for 1996, which is the subject of the instant petition, the Court finds a different conclusion. Income payments received by Petitioner in 1996 should be reflected in Petitioner's ITR for 1996 regardless of its source, be it from its commercial or non-commercial operation. Sections 27 to 29 (now Sections 31 to 35) of the Tax Code clearly enumerated what are included in the gross income of the taxpayer and what should be excluded. Thus, since Petitioner failed to show to the Court that the income payments it received from Procter and Gamble Philippines are excluded in the definition of gross income, and considering that Petitioner is not yet entitled to an income tax holiday in 1996, the same should be subject to income tax, as well as withholding taxes. In other words, unless specifically excluded, any amount, proceeds or property received by the Petitioner in 1996 should form part of his taxable income.

Moreover, since the instant case involved a claim for refund of creditable withholding taxes, it is but appropriate to state once more the requisites laid down by the Supreme Court in the case of **Citibank N.A. vs. Court of Appeals and Commissioner of Internal Revenue, 280 SCRA 459,** to wit:

1) That the taxpayer filed its claim for refund within the two (2) year period prescribed under Section 230 (now Section 229) of the Tax Code;

2) That it was shown in the return that the income payment received was declared as part of the gross income (Section 10, Revenue

> Regulations No. 6-85 [now Revenue Regulations No. 12-94] ACCRA Investment Corporation vs. Court of Appeals, 204 SCRA 957); and

3) That the fact of withholding is established by a copy of statement (BIR Form 1743.1) duly issued by the payor (withholding agent) to the payee, showing the amount paid and the amount of tax withheld therefrom *(ibid)*.

There is no doubt that Petitioner complied with the first and third requirements abovestated. It filed its corporate annual income tax return for 1996 with the Respondent on May 22, 1997 (Exh. B), its administrative claim for refund on April 4, 1997 (Exh. F) and the instant Petition for Review with this Court on November 20, 1998, so the dates of the administrative claim for refund and the judicial claim for refund falls within the two-year period from the date of payment of the tax. The fact of withholding was likewise established by Petitioner when it presented in evidence the Certificate of Creditable Income Tax Withheld at Source for the year 1996 issued by its withholding agent, Procter and Gamble Philippines (Exh. E).

However, with regard to the second requirement, the Court finds that Petitioner failed to comply with the same. The income upon which the taxes were withheld were not declared in the annual income tax return of the Petitioner for the year 1996 (Exh. A). It merely stated in its 1996 ITR that it had no commercial operation during said period without mentioning the income payments of P93,628,801.77 made by Procter and Gamble Philippines to Petitioner in 1996, upon which the amount of P936,288.01, which is the subject of the instant petition, was withheld. Clearly Petitioner's omission to declare in its 1996 ITR the income payments made by Procter and Gamble Philippines in 1996 will bar it from the recovery/refund of the withholding taxes allegedly withheld by the said withholding agent. If the said income payments were properly reported by Petitioner as income for 1996, the same may produce a taxable amount on the part of Petitioner instead of a refund.

Petitioner's invocation of BIR Ruling No. DA-460-96 dated December 4, 1996, quoted below, which states that the income payments made by Procter and Gamble Philippines, Inc. shall not be subject to 1% expanded withholding tax is unavailing in the case at bar.

> Stepan Philippines, Inc.
> 17th Floor UCPB Building
> Makati Avenue, Makati City
>
> Attn.: Ms. Ingrid S. Dungca
> Assistant Treasurer
>
> Gentlemen:
>
> This refers to your letter dated October 17, 1996 requesting for the issuance of a certificate of exemption from the creditable withholding tax of 1% on income payments made to you as a local supplier of goods.
>
> Documents submitted show that you are a BOI-registered pioneer enterprise and holder of a Certificate of Registration No. DP 94-422 dated October 24, 1994 for the manufacture of coco fatty alcohol surfactants (CFAS); that you started commercial operations on July 1994; and that you are the regular supplier of CFAS of Procter and Gamble Philippines, Inc., one of the top 5,000 corporations in the Philippines.
>
> In reply, please be informed that Section 4(b)(2) of Revenue Regulations No. 6-85, as amended by Revenue Regulations No. 12-94, provides that the withholding tax therein prescribed shall not apply to income payments to persons enjoying exemption from payment of income taxes pursuant to the provisions of the Omnibus Investments Code of 1987, as amended. Since you enjoy exemption from income taxes pursuant to the provisions of Section 39(a)(1) of the Omnibus Investments Code of 1987, the income payments made to you as the

> local supplier of Procter and Gamble Philippines, Inc. shall not be subject to 1% expanded creditable withholding tax prescribed under Revenue Regulations No. 12-94, (BIR Rulings No. 50(b)/000-00/163-94 dated December 2, 1994; and UN 339-94 dated December 6, 1994.
>
> Very truly yours,
>
> Alicia P. Clemeno
> Asst. Commissioner
> (Legal Service)
>
> By:
> (Sgd.) Alicia L. Tomacruz
> Head Rev. Executive Assistant
> (Legal Service)

As stated in the aforesaid ruling, Petitioner represented itself to have started its commercial operation in July, 1994, hence the ruling stated it is exempt from payment of income tax for the year 1996, including withholding taxes, pursuant to the provisions of Section 39(a)(1) of the Omnibus Investments Code of 1987 (E.O. 226). However, as discussed earlier, the BOI Board, per its minutes dated September 4, 1997, amended the date of the start of commercial operation of Petitioner from July, 1994 to July, 1997 (p. 70 docket, TSN, April 23, 1999, p. 40), therefore, it is only from July, 1997 that the six year income tax holiday will become effective. Accordingly, the income payments in 1996 made by Procter and Gamble Philippines, Inc. to Petitioner is subject to income tax and withholding tax, as Petitioner is not yet entitled to any income tax holiday as of the year 1996.

Well settled is the rule that tax refunds partake of the nature of tax exemptions. As such, they are regarded as in derogation of sovereign authority and is to be construed in *strictissimi juris* against the person or entity claiming the exemption **(Commissioner of**

Internal Revenue vs. Procter and Gamble Philippines Mfg., Corp., 204 SCRA 377; Commissioner of Internal Revenue vs. Rio Tuba Nickel Mining Corporation, 207 SCRA 549). Likewise, in an action for refund, the burden of proof is upon the claimant to establish its right to claim the tax refund. Since in the case at bar, Petitioner failed to discharge its burden, the Court has no other recourse but to deny the claim for refund.

IN THE LIGHT OF ALL THE FOREGOING, the instant Petition for Review is **DISMISSED** for lack of merit. No costs.

SO ORDERED.

RAMON O. DE VEYRA
Associate Judge

WE CONCUR:

ERNESTO D. ACOSTA
Presiding Judge

AMANCIO Q. SAGA
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