REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

MAR FISHING CO., INC.,
Petitioner,

-versus -

C.T.A. CASE NO. 4287

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

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D E C I S I O N

This case involves an assessment of P311,229.99 inclusive of surcharge and interest for alleged deficiency withholding tax at source on technical service fees for the year 1982 due to British Columbia Packers, Ltd. of Canada, a non-resident foreign corporation.

Petitioner, Mar Fishing Co., Inc. (MFCI), is a domestic corporation engaged in the business of tuna fishing and canning for export. In the course of its business operation, it executed a three-year contract with British Columbia Packers, Limited (BCPL), a Canadian fishing company, for technical services to be rendered by BCPL to petitioner in the area of quality control, maintenance and other related matters. Under the agreement, petitioner shall pay

BCPL the amount of 60,000.00 Canadian dollars or equivalent to P430,500.00 per year.

In a letter dated July 27, 1987, received by petitioner on August 5, 1987, respondent assessed against petitioner the amount of P311,729.99 inclusive of surcharge and interest for alleged deficiency withholding tax at source for the year 1982. In a letter dated August 6, 1987 petitioner protested the assessment on the ground that the technical services fees supposedly paid to British Columbia Packers, Ltd. of Canada were merely accrued in the books of petitioner but were not actually paid. On March 28, 1988, respondent served upon petitioner a warrant of levy of real property which seeks to enforce the collection of the said deficiency tax. In a letter dated April 4, 1988, petitioner requested for the cancellation of the warrant of levy as well as the assessment in question. However, in a letter dated May 25, 1988, which petitioner received on June 9, 1988, respondent denied the request for cancellation of the assessment and the warrant of levy.

Hence, on July 8, 1988, petitioner filed the instant petition for review. Petitioner alleged that although the said technical service fees were accrued in the books of the corporation they were never paid to BCPL. In fact, in view of financial losses incurred by petitioner, said fees were condoned or waived by BCPL. Since no payment was actually effected and BCPL did not receive any income, there arose no legal obligation on the part of BCPL to pay the tax nor on the part of the petitioner to withhold the same.

On the other hand, respondent in his answer maintains that the liability to withhold and pay income tax attaches at the time of accrual and not at the time of actual remittance or payment thereof. He cited Section 54 of the Tax Code then applicable which expressly provides that payment of withholding tax-at-source shall be made within twenty-five (25) days from the close of each calendar quarter. As reported by a BIR examiner, the amount of P413,196.00 has already been paid to BCPL.

Based on the records and evidences presented, we agree with the petitioner that the said technical service fees were never paid to BCPL. This conclusion is very evident from the following documentary evidence presented by the petitioner during the hearing, namely:

Exhibit "B" - notarized declaration of BCPL Vice President for Finance Mr. Morley Chang dated November 1, 1988 executed at the City of Vancouver, Canada to prove that technical fee was never remitted and in fact condoned/waived;

"C" - Letter dated November 15, 1988 of Gregorio R. Suarez, Director of Foreign Exchange Regulation Department of the Central Bank to prove that there was no application made for remittance of fees to BCPL during the year 1982;

"D" - Certification dated November 22, 1988 of Joaquin, Cunanan and Company attesting that no technical service fees were remitted by the petitioner for the year 1982;

"E" - Certification under oath dated April 4, 1988, by Mr. P.P. Paulino, Vice-President of Mar Fishing Company, that the said fees were merely accrued in the books of the company but were not paid.

Respondent for his part, never presented any evidence to controvert said facts. In fact, he did not even present the BIR examiner who alleged that payment of the technical service fees was actually made. On the contrary, respondent submitted his case based on the pleadings and records of the case and did not even bother to submit any memorandum.

The remaining and only issue presented before this Court for resolution is whether or not petitioner is liable for deficiency withholding tax at source on technical service fees set up or accrued as payable to non-resident foreign corporation when said fees were not actually remitted and paid but were subsequently waived or condoned by the payee thereof.

The pertinent provisions of law involved here are Section 53(e)(2) (now Section 50) and Section 54(a)(b)(c)(d)(e)(f) (now Section 51) of the National Internal Revenue Code quoted hereunder:

> Section 53. Withholding of tax at source. x x x.
>
> xxx xxx xxx
>
> (e) Non-resident aliens and foreign corporations. x x x.
>
> (2) Non-resident foreign corporations.- In the case of foreign corporations subject to tax under this Title, not engaged in trade or business within the Philippines, there shall be deducted and withheld at the source in the same manner and upon the same items as provided in subsection (b) (1) of this section, as well as on remunerations for technical services or otherwise, a tax equal to thirty-five per centum (35%) thereof: Provided, That interest on foreign loans shall be subject to withholding tax of fifteen per centum (15%). This tax shall be returned and paid in the same manner and subject to the same conditions as provided in Section 54. This deduction and withholding shall not be required in the case of reinsurance premiums ceded to foreign insurance corporations not engaged in trade or business in the Philippines.
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> Section 54. Returns and payment of taxes withheld at source. - (a) Quarterly returns and payment of taxes withheld. - Taxes deducted and withheld under Section fifty-three 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 Minister 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. <u>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</u>. (As amended by Batas Pambansa Blg. 41.) (Underscoring supplied)

(b) Penalties for failure to render returns; for rendering false or fraudulent returns; for non-payment of taxes withheld.- The surcharges prescribed in Section seventy-three of this Title in cases of failure to render returns, for filing false or fraudulent returns and for failure to pay tax shall apply to failure to file returns or pay the tax required under this Section. In case the taxes deducted and withheld are not paid within the time prescribed, there shall be added to the amount of the unpaid tax a surcharge of twenty-five per centum plus interest at the rate of twenty per centum per annum from the date the same became due until paid. If the withholding agent is the government or any of its agencies, political subdivisions or instrumentalities, or is a government owned or controlled corporation, the employee thereof responsible for the withholding and remittance of the tax shall be personally liable for the surcharge and interest imposed herein. (As amended by P.D. No. 1773.)

(c) Statement of income payments made and taxes withheld.- Ever withholding agent required to deduct and withhold taxes under Section fifty-three shall furnish each recipient, in respect to his or its receipts during the calendar quarter or year, a written statement showing the income or other payments made by the withholding agent during such quarter or year, and the amount of the tax deducted and withheld therefrom, simultaneously upon payment at the request of the payee, but not later than the 20th day following the close of the quarter in the case of corporate payee, or not later than March 1 of the following year in the case of individual payee for creditable withholding taxes. For final withholding taxes, the statement should be given to the payee on or before January 31 of the succeeding year. (As amended by Batas Pambansa Blg. 41.)

(d) Annual returns.- Ever withholding agent required to deduct and withhold taxes under Section fifty-three shall submit to the Commissioner of Internal Revenue a reconciliation statement of quarterly payments and list of payees and income payments. In the case of final withholding taxes, the return shall be filed on or before January 31 of the succeeding year, and for creditable withholding taxes, not later than March 1 of the following the year for which the annual report is being submitted. This return, if made and filed in accordance with regulations approved by the Minister of Finance, shall be sufficient compliance with the requirements of Section seventy-seven of this Title in respect to the income payments. (Ibid.)

> The Commissioner may, by regulations, grant to any withholding agent a reasonable extension of time to furnish and submit the return required in this subsection. (Ibid.)
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> (e) Surcharge and interest for failure to deduct and withhold.- If the withholding agent, in violation of the provisions of the preceding section and implementing regulations thereunder, fails to deduct and withhold the amount of tax required under said section and regulations, he shall be liable to pay in addition to the tax required to be deducted and withheld, a surcharge of fifty per centum if the failure is due to willful neglect or, with intent to defraud the Government, or twenty-five per centum if the failure is not due to such causes, plus interest at the rate of fourteen per centum per annum from the time the tax is required to be withheld until the date of assessment. (Ibid.)
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> (f) Income of recipient.- Income upon which any creditable tax is required to be withheld at the source under Section 53 shall be included in the return of its recipient but any excess of the amount of tax so withheld over the tax due on his return shall be refunded to him subject to the provisions of Section 295; if the income tax collected at source is less than the tax due on his return, the difference shall be paid in accordance with the provisions of Section 51. (As amended by Batas Pambansa Blg. 41.)

In accordance with the aforementioned provisions of the National Internal Revenue Code, a tax equivalent to 35% of the remunerations for technical services or other income due a non-resident foreign corporation shall be deducted and withheld at source. The corresponding 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 tax shall be filed and the payment made not later than the last day of the month following the close of the quarter during which the withholding was made. For failure to deduct, withhold, file and pay the tax, a corresponding penalty is provided for by the law. Under subsection (f) of Section 54, any income upon which a creditable tax has been withheld, the recipient is required to include such income in his return. Any excess of the amount of tax so withheld over the tax due on his return shall be refunded to him but if the creditable withholding tax is less than the tax due, the difference shall be paid to the Bureau of Internal Revenue. Necessarily, in case of withholding tax on income due a non-resident foreign corporation, the income is first accrued in the books of the withholding agent pending actual remittance abroad. For some reason or another, delay in actual remittance occurs and the determination when the tax is due became an issue in many previous cases.

This Court had the occassion to interpret the aforequoted provisions of the Tax Code and to pass upon similar issues in the following cases, namely: *Western Palawan Timber Corporation vs. The Commissioner of Internal Revenue*, CTA Case No. 3544; *Dillingham (Philippines) Inc., vs. The Commissioner of Internal Revenue*, CTA Case No. 3139, affirmed by the Court of Appeals in CA-GR 20425 dated May 31, 1990; *Bayer Pharmaceuticals, Inc. vs. The Commissioner of Internal Revenue*, CTA Case No. 2846, March 16, 1979, affirmed by the Supreme Court in GR No. 72054 dated Oct. 10, 1986; and lately the case of *Wyeth Suaco Laboratories vs. The Commissioner of Internal Revenue*, CTA Case No. 3981, affirmed by the Court of Appeals in CA-GR SP. No. 16111 dated May 23, 1991.

In all the above cases cited except the Bayer case, this Court has consistently held that the withholding taxes on various income due non-resident foreign taxpayers are payable at the time of accrual of said income and not at the time of actual remittance. In the Bayer case, in view of the different situation involved, this Court has deviated from the above ruling and held that the withholding tax is not due on accrual but on actual remittance. This is so because of Central Bank restrictions which prevented the withholding agent to remit earlier the income due the non-resident foreign taxpayer. The decision of this Court lies not only on the provisions of law involved but also on equity and fair play. If the withholding agent and the non-resident foreign taxpayer have in fact recognized in the books income due the latter by reason of their contract or agreement and in fact have accrued the same, the government to which the corresponding tax is due should not be prejudiced by the laxity, delay or negligence of the withholding agent in remitting the income abroad. Withholding taxes should immediately be paid 'n respondent within the period provided under Section 54 aforequoted. Along the same principle, if the withholding agent who wishes to remit the income abroad is prevented by the government to do so, it is but equitable that he should not be held liable immediately but should wait until such time the withholding agent can comply with his remittance obligation. This is so because the government itself is the one who prevented the taxpayer from receiving the "gains, profit or income", equitably it should not ask for the tax due.

However, the instant case is different from the rest of the cases aforementioned. Unlike the Bayer case and the other cases cited, the income due the non-resident foreign corporation in the instant case was never remitted for it was condoned or waived by the recipient BCPL due to substantial financial losses by MFCI. Basic as it is, if there is no income received, there is no tax to be paid. Withholding tax is a system introduced by the government to ensure collection of taxes due, especially considering the difficulties it may encounter in collecting the same as in the case of a non-resident foreign corporation without a branch or office in the Philippines. If the income from which tax shall be imposed was not actually realized, no tax may be collected therefrom. Inasmuch as the amount of P413,196.00, the technical service fee due the BCPL, was condoned by it, the same may be considered as a gift or donation to MFCI subject to gift tax as of taxable year 1988, the year said income was waived by BCPL in favor of MFCI. This manner of treating condonation as gift is provided for under Section 50 of Revenue Regulations No. 2, issued by the Secretary of Finance upon recommendation of the Commissioner of Internal Revenue, quoted hereunder:

> "The cancellation and forgiveness of indebtedness may amount to a payment of income, to a gift, or to a capital transaction, dependent upon the circumstances. If, for example, an

individual performs services for a creditor who, in consideration thereof, cancels the debt, income to that amount is realized by the debtor as compensation for his service. If, however, a creditor merely desires to benefit a debtor and without any consideration therefor cancels the debt, the amount of the debt is a gift from the creditor to the debtor and need not be included in the latter's gross income. If a corporation to which a stockholder is indebted forgives the debt, the transaction has the effect of the payment of a dividend." (Underscoring supplied)

WHEREFORE, this instant assessment is hereby dismissed, without prejudice to the determination by the respondent of the gift tax liability of the petitioner and British Columbia Packers Ltd. (BCPL) in accordance with the provisions of Sections 101 and 102 (now Sections 91 and 92) of the National Internal Revenue Code.

No pronouncement as to cost.

SO ORDERED.

Quezon City, Metro Manila, October 4, 1991.

Ernesto D. Acosta
ERNESTO D. ACOSTA
Associate Judge

WE CONCUR:

ALEX Z. REYES
Presiding Judge

CONSTANTE C. ROAQUIN
Associate Judge

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 the Court of Tax Appeals in accordance with Section 13, Article VIII of the Constitution.

ALEX Z. REYES
Presiding Judge
Court of Tax Appeals