Republic of the Philippines
COURT OF TAX APPEALS
Quezon City

SECOND DIVISION

ISUZU PHILIPPINES, INC., Petitioner,	**C.T.A. CASE NO. 6205**
	Members :
- versus -	**Castañeda, Jr.**, *Chairman* **Uy**, and **Palanca-Enriquez**, JJ.
COMMISSIONER OF INTERNAL REVENUE, Respondent.	Promulgated: JUN 17 2005

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DECISION

This Petition for Review seeks the cancellation of four (4) internal revenue tax assessments representing deficiency value-added tax, expanded withholding tax, final withholding tax and documentary stamp tax in the total amount of P50,277,437.00 for the calendar year ended December 31, 1997.

Petitioner is a corporation duly organized and existing under and by virtue of laws of the Republic of the Philippines with office address at 114 Technology Avenue, Laguna Technopark Phase II, Biñan, Laguna. It is engaged in the assembly and production of vehicles *(Exhibit 2)*.

On February 2, 2000, petitioner received a Formal Letter of Demand with the attached Details of Discrepancies and four (4) Assessment Notices issued by the Enforcement Service of the Bureau of Internal Revenue, through its Assistant

Commissioner, Percival T. Salazar, covering the following 1997 deficiency tax assessments: *(Exhibits B, C, D, E and F)*

	Basic	Surcharge	Interest	Compromise	Total
Deficiency Value-Added Tax (ST-VAT-97-0269-2000)	P 315,672.64		P 121,941.56	P 16,000.00	P 453,614.20
Deficiency Expanded Withholding Tax (ST-EWT-97-0270-2000)	1,962,547.34		758,134.00	25,000.00	2,745,681.34
Deficiency Final Withholding Tax (ST-EWT-97-0271-2000)	13,178,727.78	P14,037,285.48	3,004,025.10		30,220,038.36
Deficiency Documentary Stamp Tax (ST-DST-97-0272-2000)	10,592,500.00	2,500,000.00	3,740,603.10	45,000.00	16,878,103.10
Totals	P26,049,447.76	P16,537,285.48	P7,624,703.76	P 86,000.00	P50,297,437.00

On March 2, 2000, petitioner through its external auditors, Sycip, Gorres, Velayo & Co., filed a protest thereon and requested the cancellation of the aforementioned deficiency tax assessments *(Exhibit G)*. On May 2, 2000, petitioner filed a supplemental protest reiterating its disagreement to the deficiency tax assessments and submitting therewith all the relevant supporting documents to refute the merit of the assessments *(pages 37 to 59, CTA records; Facts Admitted, par. 5)*.

Alleging inaction on the part of the respondent, petitioner timely filed the instant Petition for Review with this Court On November 28, 2000 pursuant to Section 228 of the National Internal Revenue Code of 1997.

The jointly stipulated issues to be resolved by the Court are the following:

1. Whether or not the petitioner has undeclared sales in the amount of P2,891,963.10 subject to VAT.

2. Whether or not petitioner is liable for VAT on its alleged unallowable input tax in the amount of P233,818.00.

3. Whether or not petitioner is liable for alleged non-withholding on the following items:

   a. Payments made to contractors in the amount of P866,212.39;
   b. Rental payments in the amount of P107,710.64;

c. Transport services in the amount of P610,531.62;
d. Purchase of transportation equipment in the amount of P199,673.93;
e. Payment made to agents and brokers in the amount of P100,900.44; and
f. Professional fees in the amount of P77,518.32.

4. Whether or not petitioner is liable for non-withholding of technical assistance, royalty payments and prizes, in the amount of P18,467,773.36;

5. Whether or not petitioner paid documentary stamp tax on the following transactions;

a. Issuance of shares covering petitioner's subscribed and paid-up capital stock; and
b. A loan between petitioner and IMA Land Holdings, Inc.

6. Whether or not there is a factual and legal basis for the deficiency VAT, EWT, FWT, DST assessments issued by the respondent against the petitioner for calendar year 1997.

We shall tackle first the sixth issue because the resolution of which will determine the necessity of discussing the rest of the issues posed by the parties.

Petitioner submits that the assessments for 1997 deficiency value-added tax, expanded withholding tax, final withholding tax and documentary stamp tax are null and void for having been issued without informing petitioner of the facts and law on which the assessments were made as required under Section 228 of the National Internal Revenue Code of 1997 and Section 3.1.4. of Revenue Regulations No. 12-99, which provide:

> SEC. 228. *Protesting of Assessment.* — When the Commissioner or his duly authorized representative finds that proper taxes should be assessed, he shall first notify the taxpayer of his findings: *Provided, however*, That a pre-assessment notice shall not be required in the following cases:
>
> xxx xxx xxx

> The taxpayers shall be informed in writing of the law and the facts on which the assessment is made; otherwise, the assessment shall be void.
>
> xxx xxx xxx
>
> Section 3.1.4. *Formal Letter of Demand and Assessment Notice.* – The formal letter of demand and assessment notice shall be issued by the Commissioner or his duly authorized representative. The letter of demand calling for payment of the taxpayer's deficiency tax or taxes shall state the facts, the law, rules and regulations, or jurisprudence on which the assessment is based, otherwise, the formal letter of demand and assessment notice shall be void.

Petitioner points out that the Formal Letter of Demand failed to disclose the bases in law and the facts on which the assessments were made. The said letter does not contain any explanation of the factual and legal bases of the assessments. It merely contained a computation of how the total alleged deficiency taxes were arrived at. Petitioner avers that the revenue examiners merely presumed that petitioner has undeclared sales and that of its income payments were not subjected either to expanded or final withholding tax.

We are not swayed with petitioner's ratiocinations.

We already ruled in a number of cases ***(Philippine Stock Exchange, Inc. vs. Commissioner of Internal Revenue, CTA Case No. 5995, October 15, 2002; Mabuhay Vinyl Corporation vs. Commissioner of Internal Revenue, CTA Case No. 5669, December 3, 2002; Philacor Credit Corporation vs. Commissioner of Internal Revenue, CTA Case No. 5674, August 14, 2003; FEB Stockbrokers, Inc. vs. Commissioner of Internal Revenue, CTA Case No. 6181, December 17, 2003; ING Bank N.V. Manila Branch vs. Commissioner of Internal Revenue, CTA Case No. 6187, August 9, 2004; Clorox International Phils., Inc. (formerly First Brands***

Philippines, Inc.) vs. Commissioner of Internal Revenue, CTA Case No. 6121, August 24, 2004; Sony Philippines, Inc. vs. Commissioner of Internal Revenue, CTA Case No. 6185, October 26, 2004; and Oceanic Wireless Network, Inc. vs. Commissioner of Internal Revenue, CTA Case No. 6111, November 3, 2004) that the purpose of Section 228 of the 1997 Tax Code in requiring that "(t)he taxpayer be informed of the law and facts on which assessment is made" is to give the taxpayer the opportunity to refute the findings of the examiner and give a more accurate and detailed explanation regarding the assessment(s) ***(Belle Corporation vs. Commissioner of Internal Revenue, CTA Case No. 5930, April 4, 2002)***. If the purpose of the said law is served in the process of issuing an assessment, then Section 228 of the National Internal Revenue Code of 1997 is deemed to have been complied with.

Records show that prior to the issuance of Formal Letter of Demand, petitioner was informed of the law and the facts on which the assessments were based. First, through the Conference Letter dated September 29, 1999 *(Exhibit 1)* and second, through the Pre-Assessment Notice dated December 23, 1999 *(page 15, BIR records)*. In both letters, petitioner was given a chance to clarify the issues arising from the investigation. The fact that petitioner was furnished of the computation and brief explanation on how the assessments for deficiency taxes were arrived at, the requirement under Section 228 is observed. We have also noted that the issues in the proposed assessments were the same issues that reached the Court.

Had petitioner not been informed of the law and the facts upon which the assessments were based during the examination, then it could not have posed any written objections or comments thereto in its protest. The computation in the Formal

Letter of Demand and the brief explanation in the Details of Discrepancies citing legal provisions are sufficient to apprise petitioner of the laws and facts involved in the assessments. Moreover, there was an informal conference set to clarify issues in the Pre-Assessment Notice.

Therefore, petitioner's defense that the documents failed to fully explain the details of the assessments holds no water. As can be gleaned from the records, respondent substantially complied with the mandate of the law and its implementing rules and regulation in the issuance of the deficiency tax assessments. We so hold that the assessments for deficiency value-added tax, expanded withholding tax, final withholding tax and documentary stamp tax issued against the petitioner are not null and void.

We now proceed to the merits of the disputed assessments. We will tackle the remaining issues as they relate to their respective deficiency tax assessments.

At this juncture, it is important to emphasize that respondent failed to include in the BIR records, substantial source documents from which the assessments were taken. Page 27 of the BIR records refers to at least three hundred fifty six (356) documents supporting the examination. But only a handful of these documents were attached to the BIR records. In fact, respondent only transmitted an eighty-three (83) page BIR records. Thus, We resolve the issues based on the evidence extant.

DEFICIENCY VALUE-ADDED TAX P453,614.20

The deficiency value-added tax assessment arose from two items of discrepancy. The first is the undeclared sales of P2,891,963.10 and second, the unallowable input tax of P26,468.33. The deficiency value-added tax was computed by the respondent as follows:

Assessment No. S-VAT-97-0269-2000

VAT		
Revenues reported per VAT Returns		P 4,627,536,383.20
Add: Undeclared Sales		*2,891,963.10*
Revenues subject to VAT per investigation		P 4,630,428,346.30
Output tax due		P 463,042,834.63
Less: Input tax credits	P462,753,630.32	
Less: Unallowable input tax	*26,468.33*	462,727,161.99
Basic VAT Deficiency		P 315,672.64
Add: Interest (1.15.2000)	P 121,941.56	
Compromise Penalty	16,000.00	137,941.56
VAT Deficiency		P 453,614.20

(Exhibit B)

a. Undeclared Sales

The examiner, Ms. Medina, in her testimony states that the correct total revenue subject to VAT of petitioner is P4,630,428,266.27, computed as follows:

Petitioner's net sales per ITR filed the same amount appearing in its Audited Financial Statement		P4,613,789,205.00
Less: a) exempt sales appearing in the Second Quarterly VAT Return filed by petitioner	P 223,818.00	
b) Zero-rated sales appearing in the Third Quarterly VAT Return filed by petitioner	1,306,522.73	1,530,340.73
Net Vatable Sale		P4,612,258,864.27
Add: a) Sales of scrap subject to VAT	P 15,135,674.00	
b) Sales of property equipment	3,033,728.00	18,169,402.00
Total Revenue subject to VAT		P4,630,428,266.27

(see respondent's Memorandum, page 532, Records; see also TSN, September 19, 2002. pp. 9-11)

Consequently, the output VAT liability of petitioner based on the alleged total revenue of P4,630,428,266.27 is P463,042,826.63 [P4,630,428,266.27 x 10%]. The examiners thereafter computed the undeclared sales of P2,891,963.10 by getting the difference between the output VAT based on alleged total revenue subject to VAT of petitioner and the output VAT declared in petitioner's 1997 VAT returns and dividing it (the difference) by 10% rate of VAT, to wit:

Output Tax on Alleged Total Revenue	P463,042,826.63
Less: Output Tax per Return	462,753,630.32
Difference	P 289,196.31
Divide by VAT rate	10%
Undeclared Sales	P 2,891,963.10

On the contrary, petitioner submits that it has no undeclared sales. The above computation was made on mere inference. The Formal Letter of Demand reveals no specific mention of any transaction which was not subjected to VAT. Hence, petitioner argues that it was left alone to determine how the undeclared sales of P2,891,963.10 was arrived at.

By tracing from its accounting records the possible sources, the following are closest approximations:

	Exhibit	Amount
Non-operating revenue	Q-1	P1,396,032.81
Foreign exchange gain		234,935.39
Sale of company car to Isuzu Auto Parts, an EPZA registered company	MM, NN, NN-1	962,000.00
Proceeds from insurance company for carnapped vehicle	Q-10	299,000.00
Total		P2,891,968.20

This Court believes that if the sources of the undeclared sales were the estimates of petitioner, then there can be no corresponding output VAT liability. As correctly reasoned out by petitioner, the above sources of income are either subject to VAT at 0% or exempt from VAT. However, based on Our evaluation of the computation, the discrepancy in sales of P2,891,963.10 comes partly from the sales of scrap and sales of property equipment.

Earlier, We have mentioned that the BIR records consisted only of 83 pages and most of the documents supporting respondent's assessments were not forwarded to this Court. Thus, for such failure of the respondent, We cannot evaluate accurately the details of the assessments. Hence, We are constrained to nullify the alleged undeclared sale of petitioner for lack of supporting documents.

b. Unallowable input tax

Respondent disallowed that portion of input taxes attributable to exempt sales in the amount of P26,468.33. The allocation of the total allowable input tax of P547,431,773.05 to exempt sales was determined in this manner:

Pro-rata Share of Input Tax of Exempt Sales to Total Sales	
Exempt Sales	P 223,818.00
Divide by Total Sales	P 4,629,066,649.45
Ratio	0.004835%
Multiply by Input Tax Claim and Allowable	P 547,431,773.05
Unallowable Input Tax	P 26,468.33

(page 8, BIR records)

In its protest, petitioner avers that the input tax of P26,468.33 pertains to exportation of vehicle sold to Isuzu Motors Asia PTE Ltd., a corporation residing in Singapore. The sale is not exempt but subject to VAT at 0%. To prove such claim petitioner presented its sales invoice marked as Exhibit H.

Hence, We are tasked to solve a corollary issue of whether the input taxes in the amount of P26,468.33 arose from exempt sales or export sales in order to determine its creditability against the output tax.

The law applicable is Section 104 of the National Internal Revenue Code of 1993. Pertinent portions of which is hereby quoted as follows:

> SEC. 104. *Tax Credits. (a) Creditable input tax.* – Any input tax evidenced by a VAT invoice or official receipt issued in accordance with Section 108 hereof on the following transactions shall be creditable against the output tax
>
> xxx xxx xxx
>
> A VAT-registered person who is also engaged in transaction subject to the value-added tax shall be allowed input tax credit as follows:
>
> (A) Total input tax which can be directly attributed to transactions subject to value-added tax; and
>
> (B) A ratable portion of any input tax which cannot be directly attributed to either activity.
>
> xxx xxx xxx
>
> (c) Determination of creditable input tax. – The sum of the excess input tax carried over from the preceding month or quarter and the input tax creditable to a VAT-registered person during the taxable month or quarter shall **be reduced** by the amount of claim for refund or tax credit for value-added tax and other adjustments, such as purchase returns or allowances and input tax attributable to exempt sale. *(Underlining supplied).*

A perusal of the BIR records reveals that petitioner is engaged in taxable sales and exempt sales. The sales of petitioner during the year 1997 based on the amended 1997 VAT returns were detailed by the examiners as follows:

AMENDED VAT RETURN

	SALES	
	AMOUNT	OUTPUT TAX
January	P 294,155,576.00	P 29,415,557.60
February	332,489,349.10	33,248,934.91
March	438,925,388.20	43,892,538.82
Taxable	P1,065,570,313.30	P106,557,031.33
Zero-rated	-	-
Exempt	-	-
Sub total	P1,065,570,313.30	P106,557,031.33
April	P 450,648,156.00	P 45,064,815.60
May	438,988,274.83	43,898,826.84
June	350,705,683.87	35,070,568.39

Taxable	P1,240,342,122.76	P124,034,210.95
Zero-rated	-	-
Exempt	***223,818.00***	-
Sub total	P1,240,565,940.76	P124,034,210.95
July	P 343,342,838.35	P 34,334,283.85
August	444,666,177.76	44,466,618.09
September	533,149,897.45	53,314,990.19
Taxable	P1,321,158,913.56	P132,115,892.13
Zero-rated	*1,306,522.73*	-
Exempt	-	-
Sub total	P1,322,465,436.29	P132,115,892.13
October	P 466,889,686.55	P 46,688,968.99
November	308,108,047.56	30,810,805.00
December	225,467,224.99	22,546,721.92
Taxable	P1,000,464,959.10	P100,046,495.91
Zero-rated	-	-
Exempt	-	-
Sub total	P1,000,464,959.10	P100,046,495.91
TOTAL SALES	P4,629,066,649.45	P462,753,630.32

(page 7, BIR records)

From the above listed sales, petitioner reported an exempt sales only in the second quarter of 1997 in the amount of P223,818.00. However, the invoice *(Exhibit H)* supporting petitioner's export sale was dated July 16, 1997 which fell on the third quarter of 1997. Said document cannot negate respondent's finding of exempt sales during the second quarter of 1997. Therefore, the amount of P26,468.33 should be disallowed as creditable input VAT pursuant to Section 104(c) of the National Internal Revenue Code of 1993.

The deficiency value-added tax for 1997 is recomputed as follows:

Revenues reported per VAT Returns		P4,627,536,383.20
Output tax due		P 462,753,638.32
Less: Input tax credits	P462,753,630.32	
Less: Unallowable input tax	26,468.33	462,727,161.99
Basic VAT Deficiency		P 26,476.33

Add: Interest (1.15.2000)		10,325.77
VAT Deficiency	P	36,802.10

The compromise penalty of P16,000.00 is not imposed as compromise implies mutual agreement which is absent in the case under consideration ***(Rightfield Property Ventures, Inc. (now known as Universal Rightfield Property Holdings, Inc.) vs. Commissioner of Internal Revenue, CTA Case No. 5972, October 16, 2003).*** The imposition of the same without the conformity of the taxpayer is illegal and unauthorized ***(Commissioner of Internal Revenue vs. Lianga Bay Logging Co., Inc., G.R. No. 35266, January 21, 1991).***

DEFICIENCY EXPANDED WITHHOLDING TAX P2,745,681.34

Respondent likewise found that certain income payments of petitioner were allegedly not subjected to expanded withholding tax. This finding was arrived at after comparing the payments reflected in the Alpha List submitted by petitioner with the expenses appearing in the financial statement. The deficiency expanded withholding tax in the amount of P2,745,681.34 is computed as follows:

	Per Alpha List	Per Financial Statement	Discrepancy	Rate Applied	Deficiency EWT
Contractors:					
COS- Outside Services		P 17,234,238.69			
COS-Repairs		25,312,868.24			
Increase in Construction in Progress		39,001,570.00			
Increase in the Cost of Buildings		41,327,902.00			
Advertising and Promotions		120,561,815.00			
Janitorial, Sec. & System Expenses		17,498,713.46			
Total	P174,315,867.90	P260,937,107.39	P86,621,239.49	1%	P 866,212.39
Rent	85,648,588.20	87,802,801.00	2,154,212.80	5%	107,710.64
Agents and Brokers-Trust & Option fees	7,992,101.20	10,010,110.00	2,018,008.80	5%	100,900.44
Transport Services-Freight in	5,100,513.00	66,153,674.50	61,053,161.50	1%	610,531.62
Purchase of Transportation Equipments	-	19,967,393.00	19,967,393.00	1%	199,673.93
Professional Fees	775,183.20	775,183.20	-		77,518.32
Total Deficiency EWT					P1,962,547.34
Add: Interest-1.26.98 to 12.31.99					758,134.00

Compromise Penalty	25,000.00
Total Due and Collectible	P2,745,681.34

(page 4, BIR records)

From the above presentation of the assessment, this Court expects petitioner to prove that the expenses appearing in its financial statement were indeed subjected to withholding tax or an explanation from its end why the discrepancies were not subjected to the required withholding tax.

We will discuss the above items chronologically.

a. Contractors

i. COS-Outside Services.

The cost of sales-outside services amounting to P17,234,238.69 was accounted by petitioner as follows:

Canteen	P 4,521,108.98	meal subsidies
Janitorial Services	5,431,336.27	1% tax
Security Services	3,812,369.19	1% tax
Shuttle Bus Services	3,469,424.25	3% tax
Total	P17,234,238.69	

(Exhibits II & JJ-3)

Based on Exhibit II, petitioner impresses upon the Court that except for the payment for the canteen services, the rest of the above-listed expenses were already subjected to expanded withholding tax at either 1% or 3%. The explanation for non-withholding of tax for canteen service is evident on the remark "meal subsidies".

With the limited documents available, this Court accepts the explanation of petitioner. Records show that respondent failed to controvert the clarification made by petitioner. In his memorandum, he merely presented the computation of the deficiency expanded withholding tax. Respondent did not bother to expound.

ii. COS-Repairs

According to petitioner, this item consists mostly of purchases of materials and chemicals needed for its plant maintenance such as rash neutralizer, local chemicals, aluminum sulfate and the like. Petitioner claims that payments for these expenses do not fall under any income payments subject to expanded withholding tax under Revenue Regulations 6-85. Petitioner offered some official receipts, delivery receipts, and its own local receiving reports to establish its cause *(Exhibits L, L-1, L-1-a, L-1-b, L-2, L-2-a, L-2-b, L-3, L-3-a, L-3-b, L-4, L-4-a, L-4-b, and L-4-c).*

Inasmuch as respondent failed to specify the provision of Revenue Regulations No. 6-85, as amended, which was not complied with by petitioner, this Court finds it acceptable to consider the above documents offered by petitioner. Respondent also did not elaborate in his memorandum on this issue. Consequently, the amount of P380,015.80 representing the total purchases supported by the above-cited exhibits is not subject to withholding tax.

iii. Increase in Construction in Progress

Petitioner offered no explanation. Hence, the amount will be considered only for purposes of the determination of deficiency expanded withholding tax.

iv. Increase in the Cost of the Buildings

The same as in discussion of sub-item a(iii).

v. Advertising and Promotions

Petitioner argues that not all payments under the above heading are subject to withholding tax. Included in this expense account are reimbursements paid to agencies, purchases of promo items to suppliers, payments to insurance companies and sponsorship which it believes are not subject to expanded withholding tax.

Petitioner presented the breakdown of the charges posted against the Advertising and Promotions account to support its contention *(Exhibits S-1-1 to S-3-1).*

After evaluation, We are convinced that petitioner satisfactorily accounted for expenses posted. The required tax on income payment accounts which should have been subjected to withholding tax was shown to have been paid. But those which refer to reimbursable expenses were not subjected to withholding tax. The latter act of petitioner is in pursuance to a number of rulings issued by the Bureau of Internal Revenue, *(BIR Ruling Nos. 28-80, 202-81, 154-84, 014-88, 345-88, 001-90, and 129-92).*

vi. Janitorial, Security & System Expenses

Petitioner explains that it was assessed twice for the account of Janitorial Services of P5,431,336.26 and Security Services of P3,812,369.19 or a total amount of P9,243,705.46. The first is when the said accounts were included in breakdown of COS-Outside Services of P17,234,238.69 (as earlier presented). And second in the present Janitorial, Sec. & System Expense account.

The double imposition is evident when the aggregate amount of P9,243,705.46 was added again to the Janitorial, Securities and Other Services in the amount of P8,255,008.00 *(Exhibit KK-3)* which results to the increased sum of P17,498,713.46.

After a meticulous perusal of the records, We agree with petitioner. Indeed, the amounts pertaining to Janitorial Services of P5,431,336.26 and Security Services of P3,812,369.19 or a total amount of P9,243,705.46 was considered twice by respondent in arriving at the deficiency expanded withholding tax. Hence, the same should not form part in the final computation of the assessment.

b. Rent

Respondent opines that the total rental payment reflected in petitioner's 1997 financial statement of P87,802,801.00 was not entirely subjected to expanded withholding tax. Thus, the difference of P2,154,212.80 representing the discrepancy between the amount of P85,648,588.20 reported in the Alpha List and the amount of P87,802,800.00 declared in the financial statement was subjected to 5% expanded withholding tax.

Petitioner contends otherwise. It maintains that only the sum of P85,648,588.20 is subject to withholding tax. The difference of P2,154,212.80 is accounted by petitioner as follows:

Account Name	Per Financial Statement	Per Alpha List	Difference
Land Lease	P83,649,195.00	P76,403,724.00	P7,245,471.00
Rent Expense	4,153,605.89	9,185,906.81	(5,032,300.92)
Sales Promotion	-	58,943.60	(58,943.60)
Total	P87,802,800.89	P85,648,574.41	2,154,226.48
Rate Applied			5%
Deficiency EWT on Rental			P 107,711.32

(Exhibit LL, inclusive of submarkings)

i. Land Lease

Petitioner avers that out of the total Land Lease of P83,649,195.00 in the financial statement, only the sum of P76,403,724.00 is subject to 5% withholding tax. The balance of P7,245,471.00 refers to Construction-in-Progress on Lease Improvements, on which a 1% withholding tax was already paid under the category of payments to contractors *(Exhibit LL-3, inclusive of submarkings).* The account Construction-in-Progress is merely reclassified to Land Lease.

The explanation of petitioner is well taken.

A perusal of its documents discloses that the sum of P7,245,471.00 pertains to payments made to contractors for fence, motorpool and site development work on which a 1% creditable tax was already withheld *(Exhibits LL-3-a-4, LL-3-a-8 and LL-3-a-12).*

ii. Rent Expense

Petitioner recognized a Rent Expense of P4,153,605.89 in its financial statement but reported a bigger amount of P9,185,906.81 in its Alpha List. Petitioner explains that the amount of P9,185,906.81 comprised of rental expenses of its expatriates and rental of other property which were subjected to 5% withholding tax. However, a portion of the tax was shouldered by the expatriates, hence, the corresponding rental was not claimed by petitioner in its financial statement.

Petitioner accounted the rent expense appearing in its financial statement as follows:

Rent Expense per Alpha List		P 9,185,906.81
Less: Deductions due to		
a. Rent expense on which withholding tax was shouldered by its expatriates	P 3,648,556.33	
b. Prepaid rent for 1998	3,252,218.78	6,900,775.11
Balance		P 2,285,131.70
Add: Other Rental Expense		
a. Hotel room accommodation for Expatriates	P 163,493.82	
b. Amortization of 1997 Rent Expense	1,704,980.37	1,868,474.19
Net Rent Expense claimed in the Financial Statement		P 4,153,605.89

(Exhibit LL-4, inclusive of submarkings)

We found the above explanation sufficient to cancel the assessment for deficiency 5% withholding tax on rental expense based on the documents on record.

iii. Sales Promotion

It appearing that petitioner did not claim any sales promotion in its financial statement, therefore, it is not a part of the amount being assessed by respondent.

c. Agents and Brokers-Trust & Option Fees

Respondent classified the payments of petitioner for Trust and Option Fees as payments to Agents and Brokers which petitioner did not subject to withholding tax.

Petitioner elaborates that trust and option fees arose from Philippine New Money Bonds transactions with Citibank, N.A. It maintains that it has no obligation to withhold tax on said fees because they are not income payments subject to withholding tax under Section 1 of Revenue Regulations No. 6-85.

Records show that Citibank, N.A. through its Foreign Currency Deposit Unit, is the registered owner of certain Philippine New Money Bonds in the aggregate amount of US$3,500,000.00. Citibank, N.A. entrusted petitioner to sell or dispose the said bonds under the terms of a Trust Agreement *(Exhibit QQ-4)*. In consideration for the rights granted under the agreement, petitioner agrees to pay Citibank, N.A. a trust fee in the amount of 1/8% per annum of the amount entrusted of US$3,500,000.00.

On June 2, 1997, the bonds were sold by petitioner to Citicorp Securities International (RP), Inc. with Call Option to repurchase at the option price of P92,312,500.00 to be exercised within June 2, 1997 to July 17, 1997 *(Exhibit QQ-3)*.

On July 17, 1997, petitioner availed of the call option. Consequently, petitioner paid Citicorp Securities International (RP), Inc. an Option Fee in the amount of P1,260,107.73 and Citibank N.A., for a Trust Fee in the amount of P14,423.83 *(Exhibits QQ, QQ-1, QQ-2 and QQ-5)*. These fees are the ones which respondent believes to be subject to withholding tax at the rate of 5%.

We do not agree with the respondent.

After evaluation of the facts, this Court is convinced that the trust and option fees paid by petitioner to Citibank N.A. and Citicorp Securities International, respectively, are not within the meaning of payments to commercial brokers and agents. The term commercial broker is defined under Section 187(t) of the 1977 Tax Code, as amended,

> "*Commercial Broker*" includes all persons, other than importers, manufacturers, producers, or bona fide employees, who for compensation or profit, sell or bring about sales or purchases of merchandise for other persons, or bring proposed buyers and seller together, or negotiate freights or other business for owners of vessels, or other means of transportation, or for shippers, or consignors or consignees of freight carried by vessels or other means of transportation. The term includes commission merchants. *(see also* ***Commissioner of Internal Revenue vs. Manila Machinery & Supply Company, 135 SCRA 8, February 25, 1985)***

Records show that the trust fee is the consideration for the rights granted by Citibank N.A, to petitioner to sell the former's Philippine New Money Bonds. On the other hand, the option fee is the payment for the privilege granted to petitioner to repurchase the said bonds within the option period. Evidently, the said income payments are not the ones contemplated under the term "Brokers and Agents" in Section 1(g) of Revenue Regulations No. 6-85.

d. Transportation Services – Freight In

Petitioner has no explanation either in its protest, petition for review or memorandum so We uphold the assessment.

e. Purchase of Transportation Equipment

Likewise, respondent imposes 1% expanded withholding tax on the value of transportation equipment for 1997 in the amount of P19,967,393.61 *(Exhibit T)*.

Petitioner explains that its purchases of transportation equipment are not subject to withholding tax. The same were bought from its production line. As proof, petitioner offered various 1997 Official Receipts and Certificates of Registration with the Land Transportation Office *(Exhibits T-2 to T-30, T-32 and T-33)*. The petitioner is reflected as the registered owner of vehicles of make Isuzu.

From the above documents, this Court agrees with petitioner that the vehicles for 1997 of make Isuzu which formed part of its transportation equipment are not subject to expanded withholding tax pursuant to Section 1(k) of Revenue Regulations No. 8-90, as amended by Revenue Regulations No. 2-91, to wit:

> Section 1. Income payments subject to creditable withholding tax and rates prescribed thereon. — Except as herein otherwise provided, there shall be withheld a creditable income tax at the rates herein specified for each class of payee from the following items of income payments to persons residing in the Philippines.
>
> "(k) Gross selling price or total amount of consideration or its equivalent paid or payable to the seller/owner <u>who is not the manufacturer thereof</u> for the sale, exchange or transfer of motor vehicles.
>
> 1. For brand new vehicles - - 1%; and
> 2. For second hand vehicles - - 2%."
>
> *(Underlining supplied)*

It follows that this particular assessment has no basis in law.

f. Professional Fees

By simply looking at the computation of the respondent, the imposition of additional withholding tax when there is no discrepancy found is unreasonable. Therefore, it should be deleted for lack of factual basis. Moreover, the examiner who made the computation admitted that she committed a mistake *(page 15, TSN, September19, 2002).*

In sum, petitioner is still liable for deficiency expanded withholding tax in the amount of P1,918,904.45, recomputed based on the available documents as follows:

		Discrepancy	Rate Applied	Deficiency EWT
Contractors	P86,621,239.49			
COS-Repairs	(380,015.80)			
Janitorial, SEC & System Expenses	(9,243,705.46)	P76,997,518.23	1%	P 769,975.18
Transportation Services-Freight in		61,053,161.50	1%	610,531.62
Total Deficiency EWT				P 1,380,506.80
Add: Interest-1.26.98 to 12.31.99				538,397.65
Total Due and Collectible				P 1,918,904.45

The compromise penalty should not be imposed in the absence of mutual agreement between the parties ***(Atlas Consolidated Mining and Development Corporation (doing business under the name Atlas-Itochu Consortium) vs. Commissioner of Internal Revenue, CTA Case No. 5671, August 29, 2002).***

DEFICIENCY FINAL WITHHOLDING TAX

On page 3 of the BIR records, the deficiency final withholding tax was arrived at in the following manner:

Kind of Income Payment Per Investigation:	Amount	Rate of Tax	Final Tax Due
Technical Assistance	P 56,149,141.90	25%	P 14,037,285.48
Royalty	17,714,262.64	25%	4,428,565.66
Prizes- Exceeding 3000	*982,660.00*	*20%*	*196,532.00*

Interest	5,962,744.46	15%	1,192,548.89
Total	P 80,808,809.00		P 19,854,932.03
Less: Payments per return			
Royalty-Isuzu Motor Asia	P 296,215.00		
Prizes-Exceeding 3000	*196,532.00*		
Interest-Foreign Corp.	894,411.67		1,387,158.67
Discrepancy			P 18,467,773.36
Add: Interest 1.26.98 to 11.10.98	P 2,924,482.72		
Compromise	25,000.00		2,949,482.72
Due and Collectible			P 21,417,256.08
Less: Partial remittance on Technical Assistance			8,238,528.30
Balance			P 13,178,727.78
Add: Surcharge (failure to file return on tech. assistance)			14,037,285.48
Interest 11.11.98 to 12.31.99			3,004,025.10
Deficiency Final Withholding Tax			P 30,220,038.36

We will discuss the above items chronologically.

a. Technical Assistance
b. Royalty

Petitioner asserts that it has withheld and remitted the taxes due on its 1997 Technical Assistance and Royalty of P73,863,404.54 as follows:

Remittance to Isuzu Motors. Ltd.				Remittance to the BIR		
Date	Exhibit	In Yen	In Peso	Date	Exhibit	Amount
10-14-98		68,049,140.00	32,954,113.20	11-10-98	V-4	P 8,238,528.00
03-31-00	U-2, incl.	42,077,507.25	21,021,555.64	04-25-00	W-4	5,255,388.91
09-29-00	U-3, incl.	22,101,780.00	12,530,712.48	10-25-00	X-4	3,132,678.12
03-30-01	U-4, incl.	10,446,372.00	10,876,094.44	04-25-01	Y-4	2,719,023.61
03-01-02	U-4, incl.	26,510,125.00	17,375,196.64	04-10-02	Z-4	4,343,799.16
Total		179,184,924.25	94,757,672.40			P23,689,418.10

While the total amount of Technical Assistance and Royalty payment per above table is P94,757,672.40 and the amount declared in its 1997 books of accounts is P73,863,404.54, the difference of P20,894,267.86 as explained by petitioner, is due to foreign exchange differential and some portion of 1998 Technical Assistance and Royalty payments *(page 23, TSN, March 6, 2003).*

Petitioner further opines that the obligation or time to withhold and pay the tax on royalties due to non-resident payees is upon actual payment of the royalty and not upon mere accrual in the books ***(Borden International Philippines, Inc. vs. The Acting Commissioner of Internal Revenue, CTA Case Nos. 3221 & 3231 dated December 23, 1987 citing the case of Bayer Pharmaceuticals, Inc. vs. Commissioner of Internal Revenue, CTA Case No. 2846 dated March 16, 1979)***. Lastly, it argues that while the said amount has been set-up in its books of accounts as a liability, the same was not claimed as a deduction from gross income under its 1997 annual income tax return *(Exhibit KK)*.

Revenue Regulations Nos. 5-82 and 2-98 provide the manner of withholding, remittance, and payment of final tax on royalty in this order:

> Revenue Regulations No. 5-82.
>
> SEC. 2. Section 3 of Revenue Regulations No. 13-78, as amended by Revenue Regulations No. 6-79 and Revenue Regulations No. 3-82 is hereby further amended to read as follows:
>
> > "Section 3. *Time of Withholding*. — The <u>obligations of the payor to deduct and withhold</u> under these regulations <u>arises at time an income</u> which subject to withholding under Section 1 hereof <u>is payable or paid."</u>
>
> Revenue Regulations No. 2-98.
>
> Section 2.57.4. *Time of Withholding*. — The <u>obligation of the payor to deduct and withhold the tax</u> under Section 2.57 of these regulations <u>arises at the time an income is paid or payable, whichever comes first</u>. The term "payable" refers to the date the obligation become due, demandable or legally enforceable.
>
> Section 2.58. RETURNS AND PAYMENT OF TAXES WITHHELD AT SOURCE. —
>
> (A) Monthly return and payment of taxes withheld at source
>
> xxx xxx xxx
>
> (2) WHEN TO FILE —

> (a) The withholding tax return, whether creditable or final, shall be filed and payments should be made within 10 days after the end of each month except for taxes withheld for December which shall be filed or before January 25 of the following year. *(Underlining supplied).*

From the foregoing regulations, the obligation of petitioner to deduct and withhold final taxes on royalty payments arises on two occasions, when the royalty is (1) paid or (2) payable.

Based on the available documents, the final tax on royalty in the case at bar arises only when the same were paid by petitioner. As clarified by petitioner, the liability for 1997 Technical Assistance and Royalty due to Isuzu Motors Limited were merely set-up in its books of accounts and were not claimed as a deduction from gross income for 1997 income tax return. We believe that there is no obligation yet to withhold a final tax on recognized liability merely set-up in taxpayer's books. Thus, the assessment for final tax on Technical Assistance and Royalty has no leg to stand on.

c. Prizes

We find it unnecessary to discuss this item. As verified, the amount was already paid by petitioner as manifested in the computation. This was also admitted by the examiner during her testimony *(page 19, TSN, September 19, 2002).*

d. Interest

Similarly, the assessment for final tax on interest has no factual basis. As admitted by respondent's witness, Ms. Medina, an error was committed in the application of tax rate *(page 19, TSN, September 19, 2002)*. Instead of the correct 15% rate of tax, she inadvertently multiplied the amount of interest income on foreign corporation of P5,982,744.45 by 20% resulting to tax due of P1,192,548.89 instead of the correct tax liability of P894,411.67. The latter amount was verified to have been paid by petitioner as evidenced by Monthly Remittance Returns of Income Taxes Withheld *(Exhibits CC and DD, inclusive of submarkings).*

Based on the foregoing discussion, there is no basis for the imposition of deficiency documentary final withholding tax on Technical Assistance, Royalty, Prizes and Interest. Hence, We will not discuss the questioned surcharge for being moot and academic.

In sum, the assessment for deficiency final tax in the amount of P30,220,038.36 should be cancelled.

DEFICIENCY DOCUMENTARY STAMP TAX P16,878,103.10

Respondent alleges that petitioner failed to pay the documentary stamp tax in its original issuance of capital stocks in the amount of P10,000,000.00 and from advances to its affiliates in the amount of P395,000,000.00. The deficiency documentary stamp tax was computed by the examiners as follows:

Capital Stock Subscribed and Issued	
Number of Shares Issued	P 1,000,000.00
Par Value	1,000.00
Capital Stock	P1,000,000,000.00
DST Due (Section 175, NIRC)	P 10,000,000.00
Add: 20% Surcharge	2,500,000.00
25% Interest (3.31.98 to 12.31.99)	3,506,850.00
Compromise Penalty	25,000.00
Due and Collectible [a]	P 16,031,850.00
Advances to Affiliates-Loan Granted to ILHI	
Loan Granted	P 395,000,000.00
DST Due (Section 180, NIRC)	P 592,500.00
Add: 20% Surcharge	-
25% Interest (3.31.98 to 12.31.99)	233,753.10

Compromise Penalty		20,000.00
Due and Collectible [b]	P	846,253.10
Total Amount Due and Collectible [a] + [b]	P	16,878,103.10

(page 2, BIR records)

Petitioner refutes the above assessment holding that it already paid the documentary stamp taxes due on the issuance of shares of stocks and loan agreements to IMA Land Holding Incorporated (ILHI).

To support its claim, petitioner presented four (4) Authorities to Accept Payment duly received by BIR's accredited collecting agent bank, PNB-Atrium Branch and San Pedro Branch *(Exhibits N, M, O, and P)* purporting payments received in the aggregate amount of P10,790,020.00. The breakdown of which are as follows:

On Shares of Stock:

Date	Payment No.	Exhibit	Amount
04-22-96	3197651	N	P 2,300,000.00
09-22-95	2501450	M	7,700,000.00
		Sub-Total	P10,000,000.00

On Loan Agreements:

Date	Payment No.	Exhibit	Amount
02-26-97	4137513	O	P 454,010.00
02-26-97	4137514	P	336,010.00
		Sub-Total	P 790,020.00
		Total	P10,790,020.00

After evaluation of the above documents, this Court is convinced that the documentary stamp taxes due on the original issuance of capital stock and loans granted to its affiliate, ILHI were indeed paid. Therefore, the 1997 deficiency assessment for documentary stamp tax has no factual basis.

WHEREFORE, the Petition for Review is hereby ***PARTIALLY GRANTED***. The assessments for 1997 deficiency final withholding tax and documentary stamp tax are ***CANCELLED*** and ***WITHDRAWN*** for lack of merit. However, the 1997 deficiency value-added tax and expanded withholding tax are hereby **UPHELD** in the following amounts:

Particulars	Basic	Interest	Total
Deficiency Value-Added Tax	P 26,476.33	P 10,325.77	P 36,802.10
Deficiency Expanded Withholding Tax	1,380,506.80	538,397.65	1,918,904.45
TOTALS	P 1,406,983.13	P 548,723.42	P 1,955,706.55

Accordingly, petitioner is **ORDERED** to **PAY** the respondent the aggregate amount of P1,955,706.55, plus 20% delinquency interest per annum from February 3, 2000 until fully paid, pursuant to Section 249(C) of the National Internal Revenue Code of 1997.

SO ORDERED.

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Acting Presiding Justice

WE CONCUR:

ERLINDA P. UY
Associate Justice

OLGA PALANCA-ENRIQUEZ
Associate Justice

CERTIFICATION

I hereby certify that this Decision was reached after due consultation among the members of this Division in accordance with the provisions of Section 13, Article VIII of the Constitution.

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Chairman-2nd Division and Acting Presiding Justice