REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY
EN BANC

MALAYAN ZURICH INSURANCE COMPANY, INC.,
Petitioner,

-versus-

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

C.T.A. EB No. 61
(C.T.A. Case No. 6474)

Present:

Acosta, P.J.
Castañeda, Jr.
Bautista,
Uy,
Casanova, and
Palanca-Enriquez, JJ.

Promulgated:

MAY 16 2005

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DECISION

BAUTISTA, J.:

This Petition for Review seeks the reversal of the Decision rendered by the Court of Tax Appeals, sitting as a Division, promulgated on September 2, 2004, and the Resolution dated December 15, 2004.

The facts are uncontroverted.

Petitioner, Malayan Zurich Insurance Company, Inc., is a corporation organized and existing under and by virtue of the laws of the Philippines, with principal offices at Yuchengco Tower, 500 Q. Paredes St., Binondo, Manila. It may be served with notices and other court processes through its counsel of record, Quiason Makalintal Barot Torres and Ibarra, at the 21st Floor, Robinsons-Equitable Tower, 4 ADB Avenue corner Poveda Street, 1605 Ortigas Center, Pasig City.

For the years 1996, 1998 and 1999, petitioner purchased several Fixed Rate Treasury Notes (FXTN's) issued by the Bureau of Treasury with the following details:

Treasury Note	ISIN #	Issue Date	Maturity Date	Principal	Interest Rate	Semi-annual Interest Payment
FXTN 7-4	PIBD0703EO44	30-May-96	30-May-03	P 4,850,000	15.375%	P 372,843.75
FXTN 7-5	PIB0703G051	25-Jul-96	25-Jul-03	P 3,500,000	15.750%	P 275,625
FXTN 10-1	PIBD1006I010	26-Sep-96	26-Sep-06	P 5,000,000	16.00%	P 400,000
FXTN 10-4	PIBD1007K042	27-Nov-97	27-Nov-07	P10,000,000	22.875%	P1,143,750
FXTN 10-7	PIBD1008KT29	26-Nov-98	26-Nov-08	P 3,500,000	17.800%	P 311,500

For the period covering May 26, 2000 to December 1, 2001, the Bureau of Treasury paid interest for the said treasury notes to petitioner, and withheld tax on such interest paid at the rate of 20% of the interest income.

Treasury Note	Interest Payment Date	Total Interest	20% Withholding Tax	Net Amount Paid to Malayan
PIBD0703E044	31-May-00	P 372,843.75	P 74,568.75	P 298,275
PIBD0703E044	01-Dec-00	P 372,843.75	P 74,568.75	P 298,275
PIBD0703E044	31-May-01	P 372,843.75	P 74,568.75	P 298,275
PIBD0703E044	1-Dec-01	P 372,843.75	P 74,568.75	P 298,275
PIBD0703G051	26-Jul-00	P 275,625	P 55,125	P 220,500
PIBD0703G051	26-Jul-01	P 275,625	P 55,125	P 220,500
PIBD1006I010	27-Sep-00	P 400,000	P 80,000	P 320,000
PIBD1006I010	26-Mar-01	P 400,000	P 80,000	P 320,000
PIBD1006I010	27-Sep-01	P 400,000	P 80,000	P 320,000
PIBD1007K042	27-May-00	P 1,143,750	P 228,750	P 915,000
PIBD1007K042	29-Nov-00	P 1,143,750	P 228,750	P 915,000
PIBD1007K042	27-May-01	P 1,143,750	P 228,750	P 915,000

PIBD1007K042	29-Nov-01	P 1,143,750	P 228,750	P 915,000
PIBD1008KT29	26-May-00	P 311,500	P 62,300	P 249,200
PIBD1008KT29	26-Nov-00	P 311,500	P 62,300	P 249,200
PIBD1008KT29	26-May-01	P 311,500	P 62,300	P 249,200
PIBD1008KT29	26-Nov-01	P 311,500	P 62,300	P 249,200
	Total Withholding	Tax	**P1,812,725**	

On April 29, 2002, petitioner filed with the respondent a claim for refund or issuance of a tax credit certificate amounting to P1,812,725.00 representing the tax withheld by the Bureau of Treasury on the FXTN's purchased by petitioner.

Unable to obtain a response from the respondent and in order to toll the running of the two-year prescriptive period, petitioner filed on April 29, 2002, a Petition for Review with the Court of Tax Appeals, sitting as a Division, praying for the refund or issuance of a tax credit certificate in the amount of One Million Eight Hundred Twelve Thousand Seven Hundred Twenty-Five Pesos (P1,812,725.00) representing alleged erroneous withholding tax by the Bureau of Treasury on interest payments made to petitioner in connection with the latter's purchase of treasury notes with a maturity of more than five (5) years. Respondent, thereafter, filed his Answer on May 23, 2002.

Petitioner anchored its claim for refund on Section 32(B)(7)(g) of the 1997 Tax Code, which provides, *viz*:

> "SEC. 32. Gross Income.-
>
> xxx xxx xxx
>
> (B) Exclusions from Gross Income.- The following items shall not be included in gross income and shall be exempt from taxation under this Title:
>
> xxx xxx xxx
>
> (7) Miscellaneous Items.-

> xxx xxx xxx
>
> (g) Gains from Sale of Bonds, Debentures or other Certificate of Indebtedness. - Gains realized from the sale or exchange or retirement of bonds, debentures or other certificate of indebtedness with a maturity of more than five (5) years.
>
> xxx xxx xxx"

On September 2, 2004, a Decision was rendered by the Court's Division denying petitioner's claim for refund. Dispositive portion reads:

> "**IN LIGHT OF THE FOREGOING**, petitioner's claim for refund of the 20% final on interest income earned by it from investments in long-term treasury notes is hereby **DENIED** for lack of merit.
>
> **SO ORDERED**."

Petitioner, thereafter, filed a Motion for Reconsideration assailing the Division's decision, which was likewise denied in a Resolution dated December 15, 2004 and received by petitioner's counsel on January 5, 2005.

On January 19, 2005, petitioner filed the instant Petition for Review assailing the Decision and Resolution rendered by the Court's Division on September 2, 2004 and December 15, 2004, respectively.

The sole issue brought for the consideration of the Court En Banc is: "Whether or not the CTA erred in ruling that the term "Gain" as used in Section 32 (B)(7)(g) of the Tax Code does not include interest."

The petition is not meritorious.

The main controversy in this case lies in the correct interpretation of the term "gains" as contemplated in Section 32(B)(7)(g) of the 1997 Tax Code.

Petitioner advances the view that the term "gain" is very broad in scope which includes the term "interest". It argues that the term "gain" should be understood in its generic and not in its restrictive sense. Accordingly, such interpretation not only deviates from the legislative intent but also runs counter to the rules on statutory construction that the statutory language should be interpreted in a generic sense and given its usual and commonly understood meaning.

To support its stance, petitioner invoked BIR Ruling No. 166-99, where, then BIR Commissioner Rualo ruled that interest income or yields or gains from the sale of bonds, debentures and certificates of indebtedness with maturities of more than five (5) years are excluded from gross income in accordance with Section 32(B)(7)(g) of the 1997 Tax Code, hence, exempt from the 20% final withholding tax on deposit substitutes.

We do not agree with petitioner's arguments.

The issue in this case is not one of first impression. Time and again, the Court's Division has consistently held that only the gain from sale of bonds, debentures or other certificates of indebtedness with a maturity of more than five years shall be exempt from income tax. Thus, not being included in the term "gains" as contemplated in Section 32(B)(7)(g) of the 1997 Tax Code, the interest income earned from investments in long-term fixed rate treasury notes are subject to the 20% final withholding tax.

Jurisprudence is replete with cases involving the correct interpretation of the word "gains" as contemplated in Section 32(B)(7)(g) of the 1997 Tax Code, and in the case of ***Nippon Life Insurance Company of the Philippines, Inc. vs. Commissioner of Internal Revenue, CA-G.R. SP No. 69224, November 15, 2002***, the guiding principle was laid down by the Court of Appeals affirming in *toto* the CTA's ruling on the issue, and held:

"The point of contention here is the interpretation of the term "gains" in Section 32(B)(7)(g) of the Tax Reform Act of 1997, which excludes gains from the sale, exchange or retirement of bonds from the computation of gross income. If so excluded, no taxes are due on such transactions. xxx

The CTA, on the other hand, ruled that "gains", as used in Section 32(B)(7)(g) refers only to those emanating from the sale of bonds, thereby, excluding "interests", in the process. It stressed the distinction between "gains derived from dealings in property" and "interests" which are classified as separate items of gross income. From this distinction, the CTA went on to conclude that only interests on long-term bonds held by individuals, whether citizens, resident aliens or non-resident aliens are tax-exempt. The interest on such bonds held by corporations, domestic or otherwise, are neither excluded from gross income nor exempt from taxes.

The CTA is absolutely correct. Income is the flow of money to an individual or corporation within a specified time, as payment for services, interests, or profits from investments. Income is the return in money from one's business, labor or capital invested. The famous analogy used by the Supreme Court described property, labor and capital as trees and income as their fruits. Thus, income is synonymous with profit or gain. Nippon used this general concept of income or gain to include interest within the meaning of Section 32(B)(7)(g). This strained interpretation suffers from serious flaws.

First, while the Tax Reform Act adhered to the above definition of income, it also classified income into the following categories: compensation for services, income derived from the conduct of business or exercise of profession, gains derived from dealings in property, interest, rents royalties, dividends, annuities, prizes and winnings, pensions, and a partner's distributive share from net income of a general professional partnership. Section 32(B)(7)(g) clearly refers to gains realized from the sale, exchange or retirement of bonds, among others, with a maturity date of more than five (5) years. There is no reason to confuse gains from sale of bonds with gains in the general sense of income. Nippon argued that the law did not qualify the term "gains" but it is impossible not to see that the law did qualify such term and restricted it to gains from sale of bonds.

Section 32(B) enumerates the exclusions from gross income. Exclusions, like tax exemptions, are highly disfavored in law. A person claiming a tax exemption must justify his claim by the clearest terms possible because an exemption from the common burden of taxation is not allowed upon vague implications but on language too plain to be mistaken. In the instant case, Nippon's claimed exclusion runs counter to the plain, unequivocal language of the law. It resorted

> to the legislative intent behind the provision to justify departure from the literal meaning but we all know this is prohibited. The only intent that must be given effect is the one expressed in the language of the statute. If a statute is clear, plain and free from ambiguity, it must be given its literal meaning and applied without attempted interpretation. To depart from the meaning expressed by the words of the statute is to alter the statute and legislate, not to interpret. A statute which is plain, clear and free from doubt is not subject to construction; there is no need for interpretation, only application.
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> In enacting the Tax Reform Act, the legislature may have intended to develop the capital market and encourage savings in long term investments but even under the restrictive interpretation that gains under the subject provision means gains from sale of bonds, debentures and other certificates of indebtedness, such legislative intent still finds full expression. Section 32(B)(7)(g) as written and as interpreted by the CTA is still an incentive to the development of the bond market because it excludes gains from sales from the computation of the gross income. This may not be as sweeping as Nippon would have wanted to but it is an incentive nonetheless, which is faithful to the legislative intent. Nippon's all or nothing stance on the exclusion of gains from bonds finds no support in either the language or intent of the law. xxx "

The afore-quoted ruling of the Court of Appeals was affirmed by the Supreme Court in a Resolution promulgated on November 19, 2003 in the case entitled ***Nippon Life Insurance Company of the Philippines, Inc. vs. Commissioner of Internal Revenue, G.R. No. 159612***.

In addition thereto, the Court's Division held that "We believe that if Congress intended to exempt interest from bonds, debentures and other certificates of indebtedness under Section 32(B)(7)(g) of the Tax Code, it would have done so in clear and specific terms. The fact that it used the term 'Gains from sale' in the aforementioned section, knowing fully well of the reference to interest under Sections 24, 25, 27 and 28 of the Tax Code shows that it did not intend to exempt such interest under the aforementioned Section 32(B)(7)(g) of Tax Code." ***(Nippon***

Life Insurance Company Philippines vs. Commissioner of Internal Revenue, CTA Case No. 6142, February 4, 2002)

It is a fundamental principle of statutory construction that words employed in a statute are interpreted in connection with, and their meaning is ascertained by reference to, the words and the phrases with which they are associated or related. Thus, the meaning of a term in a statute may be limited, qualified or specialized by those in immediate association. ***(Ang Bagong Bayani-OFW Labor Party vs. Commission on Elections, G.R. No. 147589 January 26, 2001; Bayan Muna vs. Commission on Elections G.R. No. 147613 June 26, 2001)***

Thus, the term "gain" as used in Section 32(B)(7)(g) must be interpreted in relation to the words to which it is associated. Under the said section, the gains excluded from gross income are the ones derived from the sale of bonds, debentures and other certificate of indebtedness and not gains derived from any other manner than sale. (***Tokio Marine Marine Malayan Insurance Company, Inc. [formerly Pan Malayan Insurance Corporation] vs. Commissioner of Internal Revenue, CA-G.R. SP No. 77639, June 29, 2004)***

Furthermore, rulings issued by the Commissioner of Internal Revenue command respect and weight and are generally adopted. These rulings, however, are not conclusive upon the courts and will be disregarded if found incorrect. This court thus, finds the ruling being relied upon by petitioner erroneous. In the case of ***Philippine Bank of Communications vs. Commissioner of Internal Revenue, G.R. No. 112024, January 28, 1999,*** the Supreme Court disregarded the application of a Revenue Memorandum Circular issued by the Commissioner of Internal Revenue and held thus:

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> "It bears stressing that Revenue Memorandum Circulars are considered administrative rulings (in the sense of more specific and les general interpretations of tax laws) which are issued from time to time by the Commissioner of Internal Revenue. It is widely accepted that the interpretation placed upon a statute by the executive officers, whose duty is to enforce it, is entitled to great respect by the courts. Nevertheless, such interpretation is not conclusive and will be ignored if judicially found to be erroneous. Thus, the courts will not countenance administrative issuances that override, instead of remaining consistent with the law they seek to apply and implement." (Underlining supplied)

It is a cardinal rule in taxation that a claim for tax refund partakes the nature of a tax exemption which cannot be allowed unless granted in the most explicit and categorical language. Being in the nature of an exemption from taxation, a claim for refund is strictly construed against the claimant and the failure to discharge said burden is fatal to the claim. ***(Emmanuel and Zenaida Aguilar vs. Commissioner of Internal Revenue, CA-G.R. SP 16432, March 30, 1990)***

WHEREFORE, there being no reversible error raised by the petitioner in its Petition for Review, the same is hereby **DISMISSED**. Accordingly, the assailed Decision and Resolution promulgated on September 2, 2004 and December 15, 2004, respectively, are hereby **AFFIRMED** in *toto.*

SO ORDERED.

LOVELL R. BAUTISTA
Associate Justice

WE CONCUR:

ERNESTO D. ACOSTA
Presiding Justice

JUANITO C. CASTAÑEDA, JR.
Associate Justice

ERLINDA P. UY
Associate Justice

CAESAR A. CASANOVA
Associate Justice

OLGA PALANCA-ENRIQUEZ
Associate Justice

CERTIFICATION

Pursuant to Section 13, Article VIII of the Constitution, it is hereby certified that the above Resolution has been reached in consultation with the members of the Court *En Banc* before the case was assigned to the writer of the opinion of this Court.

ERNESTO D. ACOSTA
Presiding Justice