REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

ESSILOR MANUFACTURING PHILIPPINES, INC.,
Petitioner,

- versus - C.T.A. CASE NO. 6178

THE COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:
MAY 14 2002

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DECISION

The instant petition seeks the refund or issuance of a tax credit certificate in the amount of P2,896,896.51 allegedly representing overpaid or overwithheld taxes on royalties for the months of September, November and December, 1998 and August, November and December, 1999.

The facts are as hereunder stated.

Petitioner is a corporation duly organized and existing under and by virtue of Philippine laws, with principal office address at SFB No. 10, Bataan Economic Processing Zone, Mariveles, Bataan. It is duly registered with the Bureau of Internal Revenue (BIR) with Taxpayer Identification No. 020-000-230-560 (paragraph 1, Stipulation of Facts).

On May 17, 1995, petitioner entered into a Third Renewal Agreement (TRA) with Essilor International S.A. (EISA), a non-resident foreign corporation organized and existing under the laws of France, effective for ten (10) years commencing on January 1, 1995 and ending on December 31, 2004 (Exhibit B). Under the said agreement, in exchange for the use and enjoyment by the licensee (herein petitioner) of the right to manufacture opthalmic lenses according to the licensor's (EISA) specifications and using the industrial property, specifically the opthalmic lenses known as ORMA 1000 optical and opthalmic lenses from Thermo Setting, the licensee shall pay the licensor royalty equivalent to the amount provided in their Renewal Agreement. On May 25, 1997, the TRA was registered with the Bureau of Patents, Trademarks and Technology Transfer, evidenced by Certificate of Registration No. 1697 (Exhibit A).

During the months of September, November and December, 1998, and August, November and December, 1998, petitioner paid royalties to EISA in the total amount of P28,968,965.02. Pursuant to paragraph 2 (b), Article 12 of the RP-France Tax Treaty which requires that the withholding tax on royalty payments to French recipients shall be 25% if the payor is not registered with the Board of Investments and engaged in preferred areas of activities, petitioner withheld and remitted to the Bureau of Internal Revenue the 25% withholding tax on royalty fees in the aggregate amount of P7,242,241.26.

On January 1, 1998, however, a Protocol which amended the RP-France Tax Treaty was already in force, reducing the final withholding tax on royalties paid by a Philippine company to a resident of France from 25% to 15%. Allegedly unaware of the amendment to the Treaty, petitioner continued to withhold and remit 25% final tax pursuant to paragraph 2 (b), Article 12 of the original provisions of the RP-France Tax Treaty, *supra*.

On October 4, 2000, petitioner, through SGV & Co., filed with the BIR a formal request for the refund or tax credit of the excess or overpaid withholding tax on royalties amounting to P2,896,896.51 (paragraph 4, Stipulation of Facts).

There being no action on the part of the respondent (paragraph 6, Stipulation of Facts), petitioner filed the instant petition on October 10, 2000 in order to toll the running of the two-year prescriptive period.

On November 20, 2000, petitioner filed a Manifestation to the effect that Essilor International and Essilor International S. A. are one and the same corporation (pages 65 and 66, CTA Records).

In his Answer filed on October 30, 2000, respondent claimed by way of Special and Affirmative Defenses that:

> "5. The alleged claim for refund is likewise subject to administrative investigation/examination by the respondent.
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> 6. Inasmuch as "taxes are presumed to have been collected in accordance with laws and regulations" (Caltex Philippines, Inc. vs. Commissioner of Internal Revenue, CTA Case No. 2871, January 29, 1986), petitioner must show that the withholding taxes on royalties, which are the subject of the instant petition, were erroneously or illegally collected.
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> 7. Claims for refund are construed strictly against the claimant for the same partake the nature of tax exemption (Commissioner of Internal Revenue vs. Ledesma, G.R. L-13509, January 30, 1970, 31 SCRA 95), hence, "A claimant has the burden of proof to establish the factual basis of his/her claim for tax credit/refund." (Citibank NA vs. Court of Appeals, 280 SCRA 459).
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> 8. It is incumbent upon the petitioner to show that it has complied with the provisions of Sections 204(c) and 229 of the National Internal Revenue Code, as amended."

On December 5, 2001, counsel for the respondent manifested that she has no witness to present, thus she submits her case based on the records.

The issues we are tasked to resolve have been jointly stipulated by the parties to be as follows:

1. Whether or not petitioner paid royalties to Essilor International for the months of September, November, and December 1998 and August, November and December 1999 in the total amount of P28,968,965.02;

2. Whether or not petitioner withheld and remitted to the BIR the amount of P7,242,241.26, representing 25% withholding tax on royalty fees paid to Essilor International based on the old provision of Article 12(2) of the RP-France Tax Treaty; and

3. Whether or not petitioner has an overpaid or over-withheld tax on royalties amounting to P2,896,896.51, for the months of September, November, December 1998 and August, November and December 1999, for applying the 25% withholding tax on royalties, instead of 15%, under the RP- France Tax Treaty, as amended by the Protocol.

For purposes of clarity, we quote the pertinent provisions of the RP-France Tax Treaty and the Protocol amending the said treaty:

"**ARTICLE 12**
Royalties

1. Royalties arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

2. However, such royalties may be taxed in the Contracting State in which they arise, and according to the law of that State. However, the tax so charged shall, provided that the royalties are taxable in the other Contracting State, not exceed:

a) in the case of the Philippines, 15 per cent of the gross amount of the royalties

(i) paid by an enterprise registered with the Philippine Board of Investments and engaged in preferred areas of activities, or

(ii) paid in respect of cinematographic films or works recorded for broadcasting or television;

b) in all other cases, 25 per cent of the gross amount of the royalties."

PROTOCOL

ARTICLE 6

Paragraph 2 of Article 12 of the Convention is deleted and replaced by the following:

2. However, such royalties may also be taxed in the Contracting State in which they arise and according to the laws of that State, but if the beneficial owner of the royalties is a resident of the other Contracting State, the tax so charged shall not exceed 15 per cent of the gross amount of the royalties (Underscoring Ours)

ARTICLE 11
Entry Into Force

(2) its provisions shall have effect for the first time,

As regards taxes withheld at source, for amounts payable on or after the first day of January of the calendar year in which the Protocol entered into force."

Clearly from the foregoing provisions, the final withholding tax on royalty payments shall not exceed 15% if the beneficial owner of the royalties is a resident of the other contracting state. In the present case, petitioner was able to establish that the recipient of the royalty payments from which it withheld the 25% final withholding tax is a corporation duly organized under the laws of France, a country which is a party to the bilateral treaty subject matter of this petition. It appearing that the respondent failed to refute and, in fact, even admitted the existence of the provisions of Articles 12, 6 and 11 of the RP-France Tax Treaty, as well as the existence of the Protocol amending the said treaty and the date of its effectivity, which reduced the rate of final withholding tax from 25% to 15%, this court has no other recourse but to give merit to the refund sought for.

We now proceed to the issues presented by the parties.

Presented below is a table showing the relevant information necessary to resolve the aforestated issues, which were taken from the copies of the machine validated monthly remittance returns of income taxes withheld by the petitioner:

Applicable Month	Exhibit	Date of Payment	Amount of Royalty	Final Tax Paid at 25%
September 1998	C & C-1	October 12, 1998	P 4,927,395.03	P 1,231,848.76
November 1998	D & D-1	December 12, 1998	4,587,824.58	1,146,956.15
December 1998	E & E-1	January 25, 1999	2,330,134.69	582,533.67
August 1999	F & F-1	September 10, 1999	8,680,764.01	2,170,191.00
November 1999	G & G-1	December 10, 1999	4,077,157.45	1,019,289.36
December 1999	H & H-1	January 25, 2000	4,365,689.26	1,091,422.31
			P28,968,965.02	P7,242,241.25

Based on the above data, petitioner was able to file the administrative and judicial claims for refund or tax credit within the two-year prescriptive period prescribed under Section 204 (C) in relation to Section 229 of the Tax Code, as amended. The date of payment of the tax is reckoned, at the earliest, on October 12, 1998, the date when petitioner paid its final tax on royalties for the month of September 1998.

Since the first and second issues are interrelated, the same shall be discussed jointly.

Petitioner has an offsetting arrangement with EISA. The amount remitted by the former is already net of the receivables or payable to the latter. Petitioner paid royalties to Essilor International for the months of September, November, and December 1998 and August, November and December 1999 in the total amount of P28,968,965.02 as evidenced by the information shown in the Schedule of Offsetting Accounts (Exhibits K-2-A-1 to K-2-A-6) as well as the bank debit advices proving the remittances of petitioner to EISA. The court ascertained that the amounts remitted to EISA tally with the difference of the total receivables and total payables as shown in the Schedule of Offsetting Accounts. The amounts of royalty paid to EISA as presented by the petitioner in its Schedule of Offsetting Accounts reconciled with the amount of royalty paid as reflected in the table presented above.

With regard to the second issue, petitioner withheld and remitted to the BIR the total amount of P7,242,241.25 representing 25% withholding tax on royalty fees paid to Essilor International as evidenced by the monthly remittance returns covering the applicable months of the claim engaged by petitioner. Moreover, the commissioned independent auditing firm, SGV & Co. (pursuant to CTA Circular 1-95, as amended) was able to verify the accuracy of the royalty payments in the sum of P28,968,965.02, from which the 25% final withholding taxes of P7,242,241.26 were based (Exhibit K-1 to K-5). The independent auditing firm noted no exception in the amount sought to be refunded. The report of the independent CPA was verified by the court to be in order.

As to the third issue, the 25% withholding tax which the petitioner remitted to the BIR for the months of September, November and December 1998, and August, November and December 1999, was based on Article 12 of the Republic of the

Philippines – France Tax Treaty, which was amended by the Protocol amending the agreement between the Government of the Republic of the Philippines and the Government of the French Republic for the avoidance of double taxation and the prevention of fiscal evasion with respect to the taxes on income. The Protocol lowered the withholding tax rate on royalties paid by a Philippine company to a resident of France from 25% to 15%. While the above Protocol was entered into force on March 31, 1998, the date when the French Embassy replied to the Department of Foreign Affairs (DFA) Note No. 972153, dated July 21, 1997, as certified by the DFA's Office of Legal Affairs Memorandum, dated April 22, 1998, the reduction in the above withholding tax rate on royalties, however, retroacted to January 1, 1998 pursuant to the Article 11 of the said Protocol (paragraph 4, Stipulation of Facts).

Based on the provisions of the aforementioned Protocol, the court agrees with the petitioner that the withholding tax rate to be used is 15% instead of 25% on royalties remitted to Essilor International for the months of September, November and December 1998, and August, November and December 1999. Thus, the petitioner overpaid its final withholding tax on royalties in the amount of P2,896,896.50, computed as follows:

Tax actually remitted to the BIR	P 7,242,241.25
Amount of Royalty (as shown in the table)	P28,968,965.02
x withholding tax rate	15%
Tax due supposed to be remitted to the BIR	P 4,345,344.75
Overpayment or over-withheld	P 2,896,896.50

WHEREFORE, in the light of all the foregoing, the court finds the instant petition meritorious and in accordance with law. **Accordingly**, respondent is hereby **ORDERED to REFUND** or in the alternative, **ISSUE A TAX CREDIT CERTIFICATE** to petitioner in the amount of P2,896,896.50 representing its overpaid final withholding taxes on royalties for the months of September, November and December 1998, and August, November and December 1999.

SO ORDERED.

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Associate Judge

I CONCUR:

ERNESTO D. ACOSTA
Presiding 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