

THE PHILIPPINE GUARANTY CO., INC., PETITIONER, VS. THE COMMISSIONER OF INTERNAL REVENUE AND THE COURT OF TAX APPEALS, RESPONDENTS.

G.R. No. 22074. April 30, 1965

Ponente: REYES, J.B.L., J.

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REYES, J.B.L., J.:

The Philippine Guaranty Co., Inc., a domestic insurance company, entered into reinsurance contracts, on various dates, with foreign insurance companies not doing business in the Philippines, namely: Imperio Compania de Seguros, La Union y El Fenix Espafiol, Overseas Assurances Corp., Ltd., Sociedad Anonima de Reaseguros Alianza, Tokio Marine & Fire Insurance Co., Ltd., Union Assurance Society Ltd., Swiss Reinsurance Company and Tariff Reinsurance Limited. Philippine Guaranty Co., Inc., thereby agreed to cede to the foreign reinsurers a portion of the premiums on insurances it has originally underwritten in the Philippines, in consideration for the assumption by the latter of liability on an equivalent portion of the risks insured. Said reinsurance contracts were signed by Philippine Guaranty Co., Inc. in Manila and by the foreign reinsurers outside the Philippines, except the contract with Swiss Reinsurance Company, which was signed by both parties in Switzerland.

The reinsurance contracts made the commencement of the reinsurers' liability simultaneous with that of Philippine Guaranty Co., Inc. under the original insurance. Philippine Guaranty Co., Inc. was required to keep a register in Manila where the risks ceded to the foreign reinsurers were entered, and entry therein was binding upon the reinsurers. A proportionate amount of taxes on insurance premiums not recovered from the original assured were to be paid for by the foreign reinsurers. The foreign reinsurers further agreed, in consideration for managing or administering their affairs in the Philippines, to compensate the Philippine Guaranty Co., Inc. in an amount equal to 5% of the reinsurance premiums. Conflicts and or differences between the parties under the reinsurance contracts were to be arbitrated in Manila. Philippine Guaranty Co., Inc. and Swiss Reinsurance Company stipulated that their contract shall be construed by the laws of the Philippines.

Pursuant to the aforesaid reinsurance contracts Philippine Guaranty Co., Inc. ceded to the foreign reinsurers the following premiums:

1953

P842,466.71

1954

721,471.85

Said premiums were excluded by Philippine Guaranty Co., Inc. from its gross income when it filed its income tax returns for 1953 and 1951. Furthermore, it did not withhold or pay tax on them. Consequently, per letter dated

April 13, 1959, the Commissioner of Internal Revenue assessed against Philippine Guaranty Co., Inc. withholding tax on the ceded reinsurance premiums, thus:

1953

Gross premium per investigation

P768,580.00

Withholding tax due thereon at 24%

P184,459.00

25% surcharge

46,114.00

Compromise for non-filing of withholding income tax return

100.00

TOTAL AMOUNT DUE & COLLECTIBLE

P230,673.00

1954

Gross premium per investigation

P780,880.68

Withholding tax due thereon at 24%

P187,411.00

25% surcharge

46,853.00

Compromise for non-filing of withholding income tax return

100.00

TOTAL AMOUNT DUE & COLLECTIBLE

P234,364.00

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Philippine Guaranty Co., Inc. protested the assessment on the ground that reinsurance premiums ceded to foreign reinsurers not doing business in the Philippines are not subject to withholding tax. Its protest was denied and it appealed to the Court of Tax Appeals.

On July 6, 1963, the Court of Tax Appeals rendered judgment with this dispositive portion:

"In view of the foregoing considerations, petitioner Philippine Guaranty Co., Inc. is hereby ordered to pay to the Commissioner of Internal Revenue the respective sums of P202,192.00 and P173,153.00 for the total sum of P375,345.00 as withholding income taxes for the years 1953 and 1954, plus the statutory delinquency penalties thereon. With costs against petitioner."

Philippine Guaranty Co., Inc., has appealed, questioning the legality of the Commissioner of Internal Revenue's assessment for withholding tax on the reinsurance premiums ceded in 1953 and 1954 to the foreign reinsurers.

Petitioner maintains that the reinsurance premiums in question did not constitute income from sources within the Philippines because the foreign reinsurers did not engage in business in the Philippines, nor did they have office here.

The reinsurance contracts however show that the transactions or activities that constituted the undertaking to

reinsure Philippine Guaranty Co., Inc. against losses arising from the original insurances in the Philippines were performed in the Philippines. The liability of the foreign reinsurers commenced simultaneously with the liability of Philippine Guaranty Co., Inc. under the original insurances. Philippine Guaranty Co., Inc. kept in Manila a register of the risks ceded to the foreign reinsurers. Entries made in such register bound the foreign reinsurers, localizing in the Philippines the actual cession of the risks and premiums and assumption of the reinsurance undertaking by the foreign reinsurers. Taxes on premiums imposed by Section 255 of the Tax Code for the privilege of doing insurance business in the Philippines were payable by the foreign reinsurers when the same were not recoverable from the original assured. The foreign reinsurers paid Philippine Guaranty Co., Inc. an amount equivalent to 5% of the ceded premiums, in consideration for administration and management by the latter of the affairs of the former in the Philippines in regard to their reinsurance activities here. Disputes and differences between the parties were subject to arbitration in the City of Manila. All the reinsurance contracts, except that with Swiss Reinsurance Company, were signed by Philippine Guaranty Co., Inc. in the Philippines and later signed by the foreign reinsurers abroad. Although the contract between Philippine Guaranty Co., Inc. and Swiss Reinsurance Company was signed by both parties in Switzerland, the same specifically provided that its provision shall be construed according to the laws of the Philippines, thereby manifesting a clear intention of the parties to subject themselves to Philippine laws.

Section 24 of the Tax Code subjects foreign corporations to tax on their income from sources within the Philippines. The word "sources" has been interpreted as the activity, property or service giving rise to the income.^[1] The reinsurance premiums were income created from the undertaking of the foreign reinsurance companies to reinsure Philippine Guaranty Co., Inc. against liability for loss under original insurances. Such undertaking, as explained above, took place in the Philippines. These insurance premiums therefore came from sources within the Philippines and, hence, are subject to corporate income tax.

The foreign insurers place of business should not be confused with their place of activity. Business implies continuity and progression of transactions^[2] while activity may consist of only a single transaction. An activity may occur outside the place of business. Section 24 of the Tax Code does not require a foreign corporation to engage in business in the Philippines in subjecting its income to tax. It suffices that the activity creating the income is performed or done in the Philippines. What is controlling, therefore, is not the place of business but the place of activity that created an income.

Petitioner further contends that the reinsurance premiums are not income from sources within the Philippines because they are not specifically mentioned in Section 37 of the Tax Code. Section 37 is not an all inclusive enumeration, for it merely directs that the kinds of income mentioned therein should be treated as income from sources within the Philippines but it does not require that other kinds of income should not be considered likewise.

The power to tax is an attribute of sovereignty. It is a power emanating from necessity. It is a necessary burden to preserve the State's sovereignty and a means to give the citizenry an army to resist an aggression, a navy to defend its shores from invasion, a corps of civil servants to serve, public improvements designed for the enjoyment of the citizenry and those which come within the State's territory, and facilities and protection which a government is supposed to provide. Considering that the reinsurance premiums in question were afforded protection by the government and the recipient foreign reinsurers exercised rights and privileges guaranteed by our laws, such reinsurance premiums and reinsurers should share the burden of maintaining the state.

Petitioner would wish to stress that its reliance in good faith on the rulings of the Commissioner of Internal Revenue requiring no withholding of the tax due on the reinsurance premiums in question relieved it of the duty to pay the corresponding withholding tax thereon. This defense of petitioner may free it from the payment of

surcharges or penalties imposed for failure to pay the corresponding withholding tax, but it certainly would not exculpate it from liability to pay such withholding tax. The Government is not estopped from collecting taxes by the mistakes or errors of its agents. [[3]]

In respect to the question of whether or not reinsurance premiums ceded to foreign reinsurers not doing business in the Philippines are subject to withholding tax under Sections 53 and 54 of the Tax Code, suffice it to state that this question has already been answered in the affirmative in *Alexander Howden & Co., Ltd. vs. Collector of Internal Revenue*, L-19392, April 11, 1965.

Finally, petitioner contends that the withholding tax should be computed from the amount actually remitted to the foreign reinsurers instead of from the total amount ceded. And since it did not remit any amount to its foreign insurers in 1953 and 1954, no withholding tax was due.

The pertinent section of the Tax Code states:

"Sec. 54. Payment of corporation income tax at source .—In the case of foreign corporation subject to taxation under this Title not engaged in trade or business within the Philippines and not having any office or place of business therein, there shall be deducted and withheld at the source in the same manner and upon the same items as is provided in section fifty-three a tax equal to twenty-four per centum thereof, and such tax shall be returned and paid in the same manner and subject to the same conditions as provided in that Action."

The applicable portion of Section 53 provides:

"(b) Non-resident aliens.—All persons, corporations and general copartnerships (companias colectivas), in whatever capacity acting, including lessees or mortgagors of real or personal property, trustees acting in any trust capacity, executors, administrators receivers, conservators, fiduciaries, employers, and all officers and employees of the Government of the Philippines having the control, receipt, custody, disposal, or payment of interest, dividends, rents, salaries, wages, premiums, annuities, compensation, remunerations, emoluments, or other fixed or determinable annual or periodical gains, profits, and income of any non-resident alien individual, not engaged in trade or business within the Philippines and not having any office or place of business therein, shall (except in the cases provided for in subsection (a) of this section) deduct and withhold from such annual or periodical gains, profits, and income a tax equal to twelve per centum hereof: Provided, That no such deduction or withholding shall be required in the case of dividends paid by a foreign corporation unless (1) such corporation is engaged in trade or business within the Philippines or has an office or place of business therein, and (2) more than eighty-five per centum of the gross income of such corporation for the three-year period ending with the close of its taxable year preceding the declaration of such dividends (or for such part of such period as the corporation has been in existence) was derived from sources within the Philippines as determined under the provisions of section thirty-seven: Provided, further, That the Collector of Internal Revenue may authorize such tax to be deducted and withheld from the interest upon any securities the owners of which are not known to the withholding agent."

The above-quoted provisions allow no deduction from the income therein enumerated in determining the amount to be withheld. Accordingly, in computing the withholding tax due on the reinsurance premiums in question, no deduction shall be recognized.

WHEREFORE, in affirming the decision appealed from, the Philippine Guaranty Co., Inc. is hereby ordered to pay to the Commissioner of Internal Revenue the sums of P202,192.00 and P173,153.00, or a total amount of P375,345.00, as withholding tax for the years 1953 and 1954, respectively. If the amount of P375,345.00 is not paid within 30 days from the date this judgment becomes final there shall be collected a surcharge of 5% on the amount unpaid, plus interest at the rate of 1% a month from the date of delinquency to the date of payment, provided that the maximum amount that may be collected as interest shall not exceed the amount corresponding to

a period of three (3) years. With costs against petitioner.

SO ORDERED.

Bengzon, C. J., Bautista Angelo, Concepcion, Reyes, J.B.L., Barrera, Paredes, Dizon and Regala, JJ., concur.

[1] Mertens, Jr., Jacob. Law On Federal Income Taxation, Vol. 8, Section 45.27.

[2] Imperial vs. Collector of Internal Revenue, L-7924, September 30, 1955.

[3] Hilado vs. Collector of Internal Revenue, 100 Phil, 288; 53 Off. Gaz., 241; Koppel (Philippines), Inc. vs. Collector of Internal Revenue, L-10550, September 19, 1961; Compañia General de Tabacos de Filipinas vs. City of Manila, L-161619, June 29, 1963.

RESOLUTION

BENGZON, J.P., J.:

The Philippine Guaranty Company, Inc. moves for the reconsideration of our decision, promulgated on April 30, 1965, holding it liable for the payment of income tax which it should have withheld and remitted to the Bureau of Internal Revenue in the total sum of P375,345.00.

The grounds raised in the instant motion all spring from movant's view that the Court of Tax Appeals as well as this Court found it "innocent of the charges of violating, wilfully or negligently, sub-section (c) of Section 53 and Section 51 of the National Internal Revenue Code." Hence, it cannot subsequently be held liable for the assessment of P375.315.00 based on said sections.

The premise of movant's reasoning cannot be accepted. The Court of Tax Appeals and this Court did not find that it did not violate Section 3(c) and 54 of the Tax Code. On the contrary, movant was found to have violated Section 53 violation was due to a reasonable cause—namely, reliance on the advice of its auditors and opinion of the Commissioner of Internal Revenue—no surcharge to the 764 PHILIPPINE REPORTS Phil. Guaranty Co., Inc. vs. Comm. of Int. Rev. and CTA tax was imposed. Section 72 of the Tax Code provides:

"Sec. 72. Surcharges for failure to render returns and for rendering false and fraudulent returns.—The Commissioner of Internal Revenue shall assess all income taxes. In case of willful neglect to file the return or list within the time prescribed by law, or in case a false or fraudulent return or list is willfully made, the Commissioner of Internal Revenue shall add to the tax or to the deficiency tax, in case any payment has been made on the basis of such return before the discovery of the falsity or fraud, a surcharge of fifty per centum of the amount of such tax or deficiency tax. In case of any failure to make and file a return or list within the time prescribed by law or by the Commissioner or other internal revenue officer, not due to willful neglect, the Commissioner of Internal Revenue shall add to the tax twenty-five per centum of its amount, except that, when a return is voluntarily and without notice from the Commissioner or other officer filed after such time, and it is shown that the failure to file it was due to a reasonable cause, no such addition shall be made to the tax. * * *"

It will be noted that the first half of the above-quoted section covers failure to file a return, willingly and/or due to negligence, in which case the surcharge is 50%. In the second part of the law it covers failure to make and file a

return "not due to willful neglect", in which case only 25% surcharge should be added. As a further concession to the taxpayer the above-quoted section provides that if "it is shown that the failure to, file it was due to a reasonable cause, no such addition shall be made to the tax".

It would, therefore, be incorrect for movant to state that it was found "innocent of the charges of violating, willfully or negligently, sub-section (c) of Section 53 and Section 54". For, precisely, the mere fact that it was exempted from paying the penalty necessarily implies violation of Section 53(c). Violating Section 53(c) is one thing; imposing the penalty for such violation under Section 72[*] is another. If it is found that the failure to file is due to a reasonable cause, then exemption from surcharge sets in but never exemption from payment of the tax due.

Since movant failed to pay the tax due, in the sum of P375,345.00, this Court ordered it to pay the same. Simply because movant was relieved from paying the surcharge for failure to file the necessary returns, it now wants us to absolve it from paying even the tax. This, we cannot do. The non-imposition of the 25% surcharge does not carry with it remission of the tax.

Movant argues that it could not be expected to withhold the tax, for as early as August 18, 1953 the Board of Tax Appeals held in the case of Franklin Baker[[1]] that the reinsurance premiums in question were not subject to withholding. On top of that, movant maintains, the Commissioner of Internal Revenue, in reply to the query of its accountants and auditors, issued on September 5, 1953 an opinion subscribing to the ruling in the Franklin Baker case. As already explained in our decision a mistake committed by Government agents is not binding on the Government.

Inasmuch as movant insists on this point in its motion for reconsideration, we shall further elaborate on the same. Section 200 of the Income Tax Regulations expressly grants protection to him only if and when he follows strictly what has been provided therein.

Section 53 (c) makes the withholding agent personally liable for the income tax withheld under Section 54. It states:

"Sec. 53 (c) Return and payment.—Every person required to deduct and withhold any tax under this section shall make return thereof, in duplicate, on or before the fifteenth day of April of each year, and, on or before the time fixed by law for the payment of the tax, shall pay the amount withheld to the officer of the Government of the Philippines authorized to receive it. Every such person is made personally liable for such tax, and is indemnified against the claims and demands of any person for the amount of any payments made in accordance with the provisions of this section."

The law sets no condition for the personal liability of the withholding agent to attach. The reason is to compel the withholding agent to withhold the tax under all circumstances. In effect, the responsibility for the collection of the tax as well as the payment thereof is concentrated upon the person over whom the Government has jurisdiction. Thus, the withholding agent is constituted the agent of both the Government and the taxpayer. With respect to the collection and/or withholding of the tax, he is the Government's agent. In regard to the filing of the necessary income tax return and the payment of the tax to the Government, he is the agent of the taxpayer. The withholding agent, therefore, is no ordinary government agent especially because under Section 53 (c) he is held personally liable for the tax he is duty bound to withhold; whereas, the Commissioner of Internal Revenue and his deputies are not made liable by law. Movant then further contends that as agent of the Government it was released from liability for the tax after it was advised by the Commissioner of Internal Revenue that the reinsurance premiums involved were not subject to withholding. It relies on the provisions of the second paragraph of Section 200 of the Income Tax Regulations, which states:

"In case of doubt, a withholding agent may always protect himself by withholding the tax due, and promptly causing a query to be addressed to the Commissioner of Internal Revenue for the determination of whether or not the income paid to an individual is not subject to withholding. In case the Commissioner of Internal Revenue decides that the income paid to an individual is not subject to withholding. The withholding agent may thereupon remit the amount of tax withheld."

The section above-quoted relaxes the application of the stringent provisions of Section 63 of the Tax Code. Accordingly, it grants exemption from tax liability, and in so doing, it lays down steps to be taken by the withholding agent, namely, (1) that he withholds the tax due, (2) that he promptly addresses a query to the Commissioner of Internal Revenue for determination whether or not the income paid to an individual is subject to withholding; and (3) that the Commissioner of Internal Revenue decides that such income is not subject to withholding. Strict observance of said steps is required of a withholding agent before he could be released from liability. Generally, the law frowns upon exemption from taxation, hence, an exempting provision should be construed strictissimi juris.[[2]]

It may be illuminating to mention here however that the Income Tax Regulations was issued by the Secretary of Finance upon his authority, "to promulgate all needful rules and regulations of the effective enforcement" of the provisions of the Tax Code.[3] The mission therefore of Section 200, quoted above, is to implement Section 53 of the Tax Code for no other purpose than to enforce its provisions effectively. It should also be noted, that Section 53 provides for no exemption from the duty to withhold except in the cases of tax-free covenant bonds and dividends.

The facts in this case do not support a finding that movant complied with Section 200. For, it has not been shown that it withheld the amount of tax due before it inquired from the Bureau of Internal Revenue as to the taxability of the reinsurance premiums involved. As a matter of fact, the Court of Tax Appeals found that "upon advice of its accountants and auditors, * * * petitioner did not collect and remit to the Commissioner of Internal Revenue the withholding tax". This finding of fact of the lower court, unchallenged as it is, may not be disturbed.[4]

The requirement in Section 200 that the withholding agent should first withhold the tax before addressing a query to the Commissioner of Internal Revenue is not without a meaning for it is in keeping with the general operation of our tax laws: payment precedes defense. Prior to the creation of the Court of Tax Appeals, the remedy of a taxpayer was to pay an internal revenue tax first and file a claim for refund later.[5] This remedy has not been abrogated, for the law creating the Court of Tax Appeals merely gives to the taxpayer an additional remedy. With respect to customs duties the consignee or importer concerned is required to pay them under protest, before he is allowed to question legality of the imposition.[6] Likewise, validity of a realty tax cannot be assailed until after the taxpayer has paid the tax under protest.[7] The legislature, in adopting such measures in our tax laws, only wanted to be assured that taxes are paid and collected without delay. For taxes are the lifeblood of government. Also, such measures tend to prevent collusion between the taxpayer and the tax collector. By questioning a tax's legality without first paying it, a taxpayer, in collusion with B.I.R. officials, can unduly delay, if not totally evade, the payment of such tax.

Ofcourse, in this case there was absolutely no such collusion. Precisely, the Philippine Guaranty Company, Inc. was absolved from the payment of the 25% surcharge for non-filing of income tax returns inasmuch as the Tax Court as well as this Court believes that its omission was due to a reasonable cause.

WHEREFORE, the motion for reconsideration is denied.

SO ORDERED.

BengzonC.J., Bautista Angelo, Concepcion, Reyes, J.B.L., Dizon, Regala, Makalintal, and Zaldivar, JJ., concur.

[*] Not Section 256 of the Tax Code as claimed by movant.

[1]Umali, Roman N., Decisions of the Board of Tax Appeals, Vol. 2, pp. 303-307.

[2]]La Carlota Sugar Central vs. Jimenez, L-12436, May 31, 1961.

[3]Section 338, National Internal Revenue Code.

[4]This case was appealed upon questions of law.

[5]Section 306, Revised Administrative Code.

[6]Section 1370, Revised Administrative Code.

[7]Section 54, Commonwealth Act 470.

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