REPUBLIC OF THE PHILIPPINES
Court of Tax Appeals
QUEZON CITY

EN BANC

COMMISSIONER OF INTERNAL REVENUE, Petitioner,	**CTA EB No. 773 (CTA Case No. 7242)**
	Present:
- versus -	**ACOSTA,** *P.J.* **CASTAÑEDA, JR., BAUTISTA, UY, CASANOVA, PALANCA-ENRIQUEZ, FABON-VICTORINO, MINDARO-GRULLA,** *and* **COTANGCO-MANALASTAS,** *JJ.*
MANILA ELECTRIC COMPANY, INC., Respondent.	**Promulgated:** NOV 13 2012 custopalinario 2:15 p.m.

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AMENDED DECISION

UY, J.:

For resolution is respondent's **"MOTION FOR RECONSIDERATION"** filed on June 5, 2012, with petitioner's **"COMMENT (RE: MOTION FOR RECONSIDERATION DATED JUNE 5, 2012)"** filed on July 17, 2012 and respondent's **"REPLY"** filed on August 13, 2012, seeking the reconsideration, reversal and setting aside of the Decision of this Court promulgated on May 8, 2012, the dispositive portion of which reads:

> "**WHEREFORE,** premises considered, the present Petition for Review is hereby **GRANTED**. Accordingly, the Decision dated December 6, 2010 and Resolution dated April 15, 2011 rendered by the Second Division in

C.T.A. Case No. 7242 are hereby **REVERSED** and **SET ASIDE**. The Petition for Review filed by MERALCO in C.T.A. Case No. 7242 is hereby **DISMISSED** for having been filed way beyond the two (2)-year prescribed period.

SO ORDERED."

In the instant Motion, respondent presents the following arguments, to wit:

1. Strictly speaking, the provisions of Section 229 of the National Internal Revenue Code (NIRC) of 1997 is not applicable in the instant case because respondent is seeking the recovery of taxes legally due and collected at the time of payment but subsequently became erroneous and excessive as a result of a Supreme Court decision;

2. The case of *Atlanta Land Corporation vs. Commissioner of Internal Revenue*,[1] which was affirmed by the Supreme Court in a Minute Resolution, wherein it was ruled that *"under Section 229 claims for refund of erroneously, illegally, excessively and wrongfully collected NIRC tax should be filed within two (2) years from the date of payment of the tax regardless of any supervening cause that may arise after payment"*, is not applicable to the instant case;

3. The two-year prescriptive period is not jurisdictional and may be suspended for reasons of equity and other special circumstances;

4. The "Special Circumstance" in the instant case merits suspension of the two (2) – year prescriptive period under Section 229 of the NIRC of 1997, as amended;

5. The principle of *solutio indebti* governs this case;

6. The instant claim for tax refund should also be granted based on equitable grounds;

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[1] CTA EB No. 79, May 23, 2006.

7. The claim-of-right doctrine under the US Tax Code is not applicable in the Philippines;

8. The refund or issuance of a tax credit certificate in the instant case should not be subject to any condition; and

9. No person shall be deprived of life, liberty, or property without due process of law, nor shall any person be denied the equal protection of the laws.

Thus, respondent, in the subject motion, prays for the following reliefs:

1. That the Court of Tax Appeals (CTA) *En Banc*, **RECONSIDER, REVERSE and SET ASIDE** its Decision promulgated on May 8, 2012;

2. That the instant Petition for Review before the CTA *En Banc* dated May 19, 2011, be **DENIED**; and

3. That the Decision dated December 6, 2010 and Resolution dated April 15, 2011 of the Second Division of this Court, **ORDERING PETITIONER TO REFUND or TO ISSUE A TAX CREDIT CERTIFICATE in favor of Respondent in the amount of Five Billion Seven Hundred Ninety Six Million Three Hundred Forty Two Thousand Seven Hundred Ninety Two Pesos and 71/100 (P5,796,342,792.71)**, corresponding to the claim for a tax refund or credit for taxable years 1994-1998 and 2000, subject to and in proportion that the refund or credit to future consumption due to the customers concerned in the average amount of P0.0167 per kilowatt hour arising from the Supreme Court's Decision in G.R. Nos. 141314 and 141369, has been actually given or credited to them by MERALCO, **BE AFFIRMED** by the Court *En Banc*.

4. Respondent prays for such other reliefs and remedies as the Court may deem just and equitable under the premises.

On the other hand, petitioner, in her Comment, counter-argues as follows:

1. As the law stands, a claim for refund filed after the two-year prescriptive period effectively bars recovery of any refundable amount, regardless of any supervening cause;

2. The two-year prescriptive period is not affected by any supervening cause, hence, the phrase *"regardless of any supervening cause".* This phrase was originally added by Presidential Decree No. 69 dated November 24, 1972 and was retained in both the 1977 and 1997 NIRC. The intent of the law is unmistakable, to establish as a condition *sine qua non* that all claims and actions for refund of any tax or penalty shall be filed within two years from the date of payment of such tax or penalty, even if the taxpayer had no cause for refund as the tax or penalty, was legally collected, and even if after the lapse of the two-year period, a supervening cause should arise which would entitle the taxpayer to refund;

3. The recourse must fail. According to petitioner, respondent should have ceased burdening the Filipino people and refunded the excess amount it collected when the Energy Regulatory Board (ERB) issued its Decision ordering the refund (₱ 0.167 per kilowatt hour) to its customers. At that point, respondent had the opportunity to claim for refund as early as 1998. Undaunted, respondent asserted a right over an income cognizant of all its consequences and possible reversal of its case before the Supreme Court;

4. There is no room to apply the rule on *solutio indebti*;

5. Section 229 of the NIRC is mandatory and imperative.

THE RULING OF THE COURT EN BANC

After a more circumspect perusal of the respective arguments of the parties, We find ***partial*** merit in respondent's Motion.

Jurisprudence is to the effect that the two-year prescriptive period under Section 229 of the NIRC of 1997 <u>may be suspended</u> for reasons of equity and other special circumstances.

In *Commissioner of Internal Revenue vs. Philippine American Life Insurance Co.* (hereinafter referred to as the *"Philam case"*),[2] the Supreme Court said:

> "...even if the two-year period had already lapsed, the same is not jurisdictional and **may be suspended for reasons of equity and other special circumstances.**" *(Emphasis supplied)*

Needless to state, the Supreme Court, by tradition and in our system of judicial administration, has the last word on what the law is; it is the final arbiter of any justifiable controversy. There is only one Supreme Court from whose decisions all other courts should take their bearings.[3] In view of these doctrinal precepts, it is not hard to discern that there can be an instance where the two-year prescriptive period under Section 229 of the NIRC of 1997 may be suspended.

The pertinent question then is this: In this case, is the two-year prescriptive period under Section 229 of the NIRC of 1997 suspended by reason of equity and other special circumstances?

The answer is in the affirmative.

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[2] G.R. No. 105208, May 29, 1995.
[3] *Barrera vs. Barrera, et al.*, G.R. No. L-31589, July 31, 1970.

The relevant facts of the case, which indicates special circumstances and calls for the application of fairness, can be easily recounted:

On December 23, 1993, respondent filed with the Energy Regulatory Board (ERB) an application for revised rates, with an average increase of ₱ 0.21 per kilo watt hour (kwh) in its distribution charge. On January 28, 1994 the ERB granted a **provisional increase** of ₱ 0.184 per kwh **subject to the condition** that in the event the ERB determines that respondent is entitled to a lesser increase in rates, all excess amounts collected by respondent shall be refunded to its customers or credited in their favor. The Commission on Audit (COA) conducted an examination of the books of accounts and records of respondent and thereafter recommended, among others, that: (1) income taxes paid by respondent should not be included as part of respondent's operating expenses and (2) the "net average investment method" or the "number of months use method" should be applied in determining the proportionate value of the properties used by respondent during the test year.

In its decision dated February 16, 1998, the ERB adopted the recommendations of the COA and authorized respondent to adopt a rate adjustment of **₱ 0.017 per kwh** for its billing cycles beginning 1994. The ERB further directed respondent to **credit the excess average amount of ₱ 0.167 per kwh to its customers** starting with respondent's billing cycles beginning February 1994. The said ruling of the ERB was affirmed by the Supreme Court in its Decision dated November 15, 2002 and Resolution dated April 9, 2003.[4] Said Decision became final and executory on May 5, 2003.

[4] G.R. Nos. 141314 and 141369.

As a result of the mandated refund or credit to future consumption of the excess of ₱ 0.167 per kwh, respondent alleged that its gross electric revenue during the years 1994-1998, and 2000 was necessarily reduced. Consequently, respondent's taxable income and income tax liability were likewise necessarily reduced for the said periods. It is for this reason that respondent, Manila Electric Company, Inc., subsequently filed before the Bureau of Internal Revenue on November 27, 2003, an administrative claim for tax refund or credit of the supposed excess income tax payments for the years mentioned.

It is apparent from the foregoing circumstances that it is only when the High Court's Decision, which became final and executory on May 5, 2003, ordering the refund or credit to future consumption of the excess of ₱ 0.167 per kwh, that the amount of the refund claim of respondent was ascertained. As similarly held in the cases of *Accra Investments Corporation vs. Court of Appeals, et al.*[5] and *Commissioner of Internal Revenue vs. Philippine American Life Insurance Co.*,[6] where the Supreme Court also counted the two-year period not from the payment of tax but from the filing of the Final Adjustment Income Tax Return when the amount of taxes to be paid or to be refunded can be ascertained. Thus, in view of said circumstances, it would be iniquitous to rule that the two-year prescriptive period under Section 229 of the NIRC of 1997 was not interrupted, but instead, that it commenced to run from date of payment of the tax sought to be refunded in the instant case.

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[5] G.R. No. 96322, December 20, 1991.
[6] G.R. No. 105208, May 29, 1995.

Simply put, while Section 229 is mandatory, the prescriptive period had not commenced to run as the same was suspended due to the special circumstances obtaining in this case.

Accordingly, We agree with the Court in Division's ruling in the assailed Decision that respondent's tax refund claim has not prescribed.

The principle of* solutio indebiti *is applicable to refund of erroneously or illegally collected or assessed tax.

In *Commissioner of Internal Revenue vs. Acesite (Phils.) Hotel Corporation*,[7] the Supreme Court clearly states that tax refunds are based on the principle of *solutio indebti*, to wit:

> "**Tax refunds are based on the principle of quasi-contract or *solutio indebiti* and the pertinent laws governing this principle are found in Arts. 2142 and 2154 of the Civil Code**, which provide, thus:
>
> > Art. 2142. Certain lawful, voluntary, and unilateral acts give rise to the juridical relation of quasi-contract to the end that no one shall be unjustly enriched or benefited at the expense of another.
> >
> > Art. 2154. If something is received when there is no right to demand it, and it was unduly delivered through mistake, the obligation to return it arises.
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> When money is paid to another under the influence of a mistake of fact, that is to say, on the mistaken supposition of the existence of a specific fact, where it would not have been known that the fact was otherwise, it may be recovered. The ground upon which the right of recovery rests is that money paid through misapprehension of facts belongs in equity and in good conscience to the person who paid it.
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> **The Government comes within the scope of *solutio indebiti* principle as elucidated in *Commissioner of Internal Revenue v. Fireman's Fund Insurance Company*,[8] where we held that: 'Enshrined in the basic legal principles is the time-honored doctrine that no**

[7] G.R. No. 147295, February 16, 2007.
[8] G.R. No. L-30644, March 9, 1987.

> **person shall unjustly enrich himself at the expense of another. It goes without saying that the Government is not exempted from the application of this doctrine.'"** *(Emphases supplied)*

Furthermore, in *Filinvest Development Corporation vs. Commissioner of Internal Revenue, et al.*,[9] the High Court declared:

> "That no one shall unjustly enrich oneself at the expense of another is a long-standing principle prevailing in our legal system. This applies not only to individuals but to the State as well. In the field of taxation where the State exacts strict compliance upon its citizens, the State must likewise deal with taxpayers with fairness and honesty. The harsh power of taxation must be tempered with evenhandedness. **Hence, under the principle of *solutio indebiti*, the Government has to restore to petitioner the sums representing erroneous payments of taxes.**" *(Emphasis supplied)*

Thus, on the basis of the foregoing jurisprudential pronouncements, it is clear that the rule on *solutio indebiti* may be applied to the refund claim of respondent.

Nevertheless, We cannot affirm *in toto*, at this juncture, the amount of tax refund granted to respondent by the Court in Division for the reason explained hereinbelow.

The Court in Division rendered an incomplete judgment.

The dispositive portion of the assailed Decision rendered by the Court *a quo* reads:

> "**WHEREFORE,** premises considered, the Amended Petition for Review is **GRANTED**, as follows:
>
> 1. Respondent's denial due to prescription of MERALCO's claim for a tax refund or credit for the taxable years 1994-1998 and 2000 is **REVERSED and SET ASIDE**;
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> 2. Respondent is **ORDERED TO REFUND or TO ISSUE A TAX CREDIT CERTIFICATE** in favor of MERALCO in the amount of

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[9] G.R. No. 146941, August 9, 2007.

> **P5,796,342,792.71**, corresponding to the claim for a tax refund or credit for the taxable years 1994-1998 and 2000, subject to and in proportion that the refund or credit to future consumption due to the customers concerned in the average amount of P0.167 per kilowatthour arising from the Supreme Court's Decision in G.R. Nos. 141314 and 141369, has been actually given or credited to them by MERALCO.
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> **SO ORDERED**." *(Underscoring supplied)*

While We agree with the Court in Division that the granting of tax refund or credit in this case is dependent upon whether respondent has indeed refunded or credited to future consumption due to its customers, a plain reading of the above-quoted dispositive portion reveals that the judgment is still subject to a condition. Particularly, the Court in Division orders petitioner to refund or issue a tax credit certificate in the amount of ₱ 5,796,342,792.71, but it is still subject to a later determination whether the refund or credit to future consumption due to respondent's customers *"has been actually given or credited to them".*

This should not be the case. The Decision of the Court in Division should have included a complete determination of the total amount of refund that herein respondent, Manila Electric Co., Inc., the petitioner thereat, is entitled to, in order to put an end to the litigation of CTA Case No. 7242.

It is well established that it is the dispositive part of the judgment that **actually settles and declares the rights and obligations of the parties, finally, definitively, and authoritatively**, notwithstanding the existence of inconsistent statements in the body that may tend to confuse. It is the dispositive part that controls, for purposes of execution.[10]

In *Ignacio, et al. vs. Hilario, et al.*,[11] the Supreme Court held:

[10] *Federal Builders, Inc. vs. Daiichi Properties and Development, Inc.*, G.R. No. 142525, February 13, 2009.
[11] G.R. No. L-175, April 30, 1946.

> "There is, however, in the decision of Judge Felix a question of procedure which calls for clarification, to avoid uncertainty and delay in the disposition of cases. In that decision, the rights of both parties are well defined under articles 361 and 453 of the Civil Code, but it fails to determine the value of the buildings and of the lot where they are erected as well as the periods of time within which the option may be exercised and payment should be made, these particulars having been left for determination apparently after the judgment has become final. **This procedure is erroneous, for after the judgment has become final, no additions can be made thereto and nothing can be done therewith except its execution. And execution cannot be had, the sheriff being ignorant as to how, for how much, and within what time may the option be exercised, and certainly no authority is vested in him to settle these matters which involve exercise of judicial discretion. Thus the judgment rendered by Judge Felix has never become final, it having left matters to be settled for its completion in a subsequent proceeding, matters which remained unsettled up to the time the petition is filed in the instant case.**
>
> For all the foregoing, the writ of execution issued by Judge Natividad is hereby set aside and the lower court ordered to hold a hearing in the principal case wherein it must determine the prices of the buildings and of the residential lot where they are erected, as well as the period of time within which the plaintiffs-respondents may exercise their option either to pay for the buildings or to sell their land, and, in the last instance, the period of time within which the defendants-petitioners may pay for the land, all these periods to be counted from the date the judgment becomes executory or unappealable. **After such hearing, the court shall render a final judgment according to the evidence presented by the parties.**" *(Emphases supplied)*

Based on the foregoing, an incomplete judgment may be defined as one which leaves matters to be settled for its completion in a subsequent proceeding[12] and does not become final.

Accordingly, We are left with no alternative but to return this case to the Court *a quo* for the key finding of fact as to amount of refund to which respondent is entitled, without any condition and with definitiveness. Needless to state, said Court must still be guided by the following principles, to wit:

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[12] Moreno's Law Dictionary, © 2000, at page 224.

> "As cases filed before this Court are litigated *de novo*, party-litigants should prove **every minute aspect** of their cases."[13] *(Emphasis supplied)*
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> "...actions for tax refund, as in the instant case, are in the nature of a claim for exemption and the law is not only construed in *strictissimi juris* against the taxpayer, but also the pieces of evidence presented entitling a taxpayer to an exemption is *strictissimi* scrutinized and must be duly proven."[14]

Pursuant to these principles vis-à-vis the determination of the specific amount of tax refund, respondent's documentary evidence should not be limited to income tax returns, financial statements, and certain journal entries, as presented in the Court below, but must also include the source documents, the kilo watt hour sales statistics on a per customer class, the bill frequency, and other pertinent data, tending to prove that respondent reported its gross electric revenues at the provisional rate of ₱ 0.184 per kwh, and a concrete showing that respondent's customers were refunded or credited of the excess average amount of ₱ 0.167 per kwh starting with respondent's billing cycles beginning February 1994.

In sum, the Court *En Banc* finds the instant Motion for Reconsideration meritorious, and should therefore, be granted, on the ground that the two-year prescriptive period under Section 229 of the NIRC of 1997 was suspended prior to the High Court's Decision in G.R. Nos. 14134 and 141369, and in the light of the applicability of the principle of *solutio indebiti* to respondent's tax refund claims.

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[13] *Dizon vs. Court of Tax Appeals, et al.*, G.R. No. 140944, April 30, 2008; *Atlas Consolidated Mining and Development Corporation vs. Commissioner of Internal Revenue,* G.R. No. 145526, March 16, 2007; and *Commissioner of Internal Revenue vs. Manila Mining Corporation,* G.R. No. 153204, August 31, 2005.

[14] *Atlas Consolidated Mining and Development Corporation vs. Commissioner of Internal Revenue*, G.R. No. 159490, February 18, 2008.

However, the assailed Decision of the Court in Division cannot be affirmed as the same is an incomplete judgment. Being so, it must be set aside in order that complete relief may be fully adjudicated by the Court *a quo*. As discussed earlier, there is still a need for the said Court to conduct further proceedings for the reception of evidence to determine the precise amount of tax refund or credit, if any, that herein respondent is entitled to, without further qualification or determination.

WHEREFORE, in light of the foregoing considerations, respondent's Motion for Reconsideration is hereby **GRANTED**. The Court *En Banc's* Decision dated May 8, 2012, which granted the instant Petition for Review, is hereby **REVERSED and SET ASIDE.**

However, the Decision dated December 6, 2010 in CTA Case No. 7242, being an incomplete judgment, and the Resolution dated April 15, 2011, both rendered by the Second Division of this Court in said case, are hereby **SET ASIDE.** Accordingly, CTA Case No. 7242 is hereby **REMANDED** to the Court of origin for further reception of evidence and for a complete determination of the specific amount of refund or tax credit, if any, to which respondent is entitled to. Thereafter, the said Court shall render judgment, declaring such specific amount of refund or tax credit, if any, to which respondent is entitled to.

SO ORDERED.

ERLINDA P. UY
Associate Justice

WE CONCUR:

ERNESTO D. ACOSTA
Presiding Justice

(with Dissenting Opinion)
JUANITO C. CASTAÑEDA, JR.
Associate Justice

LOVELL R. BAUTISTA
Associate Justice

CAESAR A. CASANOVA
Associate Justice

(with Separate Dissenting Opinion)
OLGA PALANCA-ENRIQUEZ
Associate Justice

ESPERANZA R. FABON-VICTORINO
Associate Justice

CIELITO N. MINDARO-GRULLA
Associate Justice

AMELIA R. COTANGCO-MANALASTAS
Associate Justice

REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
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EN BANC

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

-versus-

MANILA ELECTRIC COMPANY, INC.,
Respondent.

CTA EB No. 773
(CTA Case No. 7242)

Present:
Acosta, *P.J.,*
Castañeda, Jr.,
Bautista,
Uy,
Casanova,
Palanca-Enriquez,
Fabon-Victorino,
Mindaro-Grulla, and
Cotangco-Manalastas, *JJ.*

Promulgated:
NOV 13 2012 2:15 p.m.

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DISSENTING OPINION

CASTAÑEDA, JR., J.:

With all due respect to my esteemed colleagues, I register my dissent to the majority opinion and vote for the DENIAL of Manila Electric Company, Inc.'s (MERALCO) "Motion for Reconsideration." This is based on the following grounds:

I. MERALCO should have claimed the overcharges as deduction from income in the year the obligation to pay accrues or arises pursuant to the NIRC of 1997.

  a. Accrual method recognizes the overcharges as expense in the year MERALCO was ordered to repay the same.

  b. The claim of right doctrine is subsumed in the NIRC of 1997.

  c. The claim of right doctrine was applied in our jurisprudence.

II. Refund should be exercised within the prescriptive period fixed by law *regardless of any supervening cause* as emphatically provided under Section 229 of the NIRC of 1997.

  a. Section 229 of the NIRC of 1997 applies to overpayment of taxes.

  b. PD 69 added the phrase *"regardless of any supervening cause."*

  c. Rationale behind the two (2) year prescriptive period.

  d. American cases have persuasive effect in our jurisdiction.

III. MERALCO failed to discharge the burden of proving its entitlement to tax refunds.

  a. Refund cannot be made to depend upon a condition.

  b. The claim was not duly proven.

  c. Submission of evidence at this stage of the proceeding is not proper.

A revisit of the facts of the case would show that MERALCO's application for the revision of its rate schedules was CONDITIONALLY GRANTED by the then Energy Regulatory Board (ERB now Energy Regulatory Commission). Notwithstanding the provisional character of the increase, MERALCO immediately imposed the new rate, recognized the income and paid the corresponding tax. As early as 1998, ERB reduced the provisional increase and ordered MERALCO to refund or credit to its customers the average amount of P0.167 per kwh. MERALCO appealed the Decision of the ERB to the Court of Appeals which ruled in its favor. However, the Supreme Court reversed the Court of Appeals' Decision and upheld the previous Decision of the ERB. On May 5, 2003, the Supreme Court's Decision became final and executory, after denying with finality MERALCO's Motion for Reconsideration therefrom.

I. Meralco should have claimed the overcharges as deduction from income in the year the obligation to pay accrues or arises pursuant to the NIRC of 1997.

Accrual method recognizes the overcharges as expense in the year Meralco was ordered to repay the same.

MERALCO's overcharges previously reported as income, subject to repayment to customers, should have been claimed as deductible expense at the time when the obligation to repay arises. Its obligation arose and ripened into a deductible expense on May 5, 2003 when the Decision of the Supreme Court attained finality.

This is in recognition of and consistent with the accrual method of accounting used by MERALCO. Accrual method allows expenses to be deducted for the taxable year in which all the events have occurred which determine the fact of liability and the amount thereof can be determined.[1] In accrual, expense is deductible when incurred and it is incurred at the time the obligation to pay arises.

The propriety of this relief is sanctioned by Sections 44 and 45 of the National Internal Revenue Code (NIRC) of 1997 which acknowledges the basic accounting principle of accrual method of income and expense recognition, it provides:

> **SEC. 44.** ***Period in which Items of Gross Income Included***. - The amount of all items of gross income shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under methods of accounting permitted under Section 43, any such amounts are to be properly accounted for as of a different period. xxx
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> **SEC. 45.** ***Period for which Deductions and Credits Taken***. - The **deductions** provided for in this Title shall be taken for the taxable year in which ***"paid or accrued"* or *"paid or incurred"***, dependent upon the method of accounting upon the basis of which the net income is computed, unless in order to clearly reflect the income, the deductions should be taken as of a different period. Xxx (emphasis ours)

The aforequoted provisions dictate that once a taxpayer receives items of gross income, the same shall be recognized as income in the taxable year of receipt. Likewise, deductions are allowed from the time the obligation was **paid or incurred** depending upon the taxpayer's method of accounting allowed by

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[1] Merten's *The Law of Federal Income Taxation*, Section 12A.152, Volume 2, (1995).

law. The accrual method *vis-à-vis* cash method of accounting was further explained in the case of *Commissioner of Internal Revenue vs. Isabela Cultural Corporation* [2] where the Supreme Court elucidated:

> The requisite that it must have been paid or incurred during the taxable year is further qualified by Section 45 of the National Internal Revenue Code (NIRC) which states that: **"[t]he <u>deduction</u> provided for in this Title <u>shall be taken for the taxable year in which 'paid or accrued' or 'paid or incurred'</u>,** dependent upon the method of accounting upon the basis of which the net income is computed . . .".
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> Accounting methods for tax purposes comprise a set of rules for determining when and how to report income and deductions. In the instant case, the accounting method used by ICC is the accrual method.
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> Revenue Audit Memorandum Order No. 1-2000, provides that **under the accrual method of accounting, expenses not being claimed as deductions by a taxpayer in the current year when they are incurred cannot be claimed as deduction from income for the succeeding year. Thus, a taxpayer who is authorized to deduct certain expenses and other allowable deductions for the current year but failed to do so cannot deduct the same for the next year.**
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> The accrual method relies upon the taxpayer's right to receive amounts or its obligation to pay them, in opposition to actual receipt or payment, which characterizes the cash method of accounting. Amounts of income accrue where the right to receive them become fixed, where there is created an enforceable liability. Similarly, **liabilities are accrued when fixed and determinable in amount, without regard to indeterminacy merely of time of payment.**
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> For a taxpayer using the accrual method, the determinative question is, when do the facts present themselves in such a manner that the taxpayer must recognize income or expense? **The accrual of income and expense is permitted when the all-events test has been met. This test requires: (1) fixing of a right to income or liability to pay; and (2) the availability of the reasonable accurate determination of such income or liability.**
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> The all-events test requires the right to income or liability be fixed, and the amount of such income or liability be determined with reasonable

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[2] G.R. No. 172231, February 12, 2007, 515 SCRA 556.

> accuracy. However, the test does not demand that the amount of income or liability be known absolutely, only that a taxpayer has at his disposal the information necessary to compute the amount with reasonable accuracy. The all-events test is satisfied where computation remains uncertain, if its basis is unchangeable; the test is satisfied where a computation may be unknown, but is not as much as unknowable, within the taxable year. **The amount of liability does not have to be determined exactly; it must be determined with "reasonable accuracy." Accordingly, the term "reasonable accuracy" implies something less than an exact or completely accurate amount.**
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> The propriety of an accrual must be judged by the facts that a taxpayer knew, or could reasonably be expected to have known, at the closing of its books for the taxable year. Accrual method of accounting presents largely a question of fact; such that the taxpayer bears the burden of proof of establishing the accrual of an item of income or deduction. (emphasis ours)

Significantly, MERALCO's liability to refund its customers has been fixed and the amount can be reasonably determined upon the finality of the Supreme Court's Decision in the consolidated cases of *Republic vs. Manila Electric Company*, G.R. No. 141314 and *Lawyers Against Monopoly, etc. vs. Manila Electric Company*, G.R. No. 141369.[3] In fact, the Supreme Court ordered the immediate refund of MERALCO's overcharges to customers, the dispositive portion of the decision reads:

> **WHEREFORE**, in view of the foregoing, the instant petitions are GRANTED and the decision of the Court of Appeals in C.A. G.R. SP No. 46888 is REVERSED. Respondent MERALCO is authorized to adopt a rate adjustment in the amount of P0.017 per kilowatthour, effective with respect to MERALCO's billing cycles beginning February 1994. Further, in accordance with the decision of the ERB dated February 16, 1998, **the excess** average amount of P0.167 per kilwatthour starting with the applicant's billing cycles beginning February 1998 **is ordered to be refunded to MERALCO's customers or correspondingly credited in their favor for future consumption.** (emphasis ours)

[3] November 15, 2002, 391 SCRA 700.

MERALCO's repayments to its customers become a deductible expense from the time the obligation to pay accrues or arises, i.e. on May 5, 2003, the date of Entry of Judgment of the above Decision. This brings about the timing of recognition of expense, the completion of the requirements for the accrual of repayments. Again, accrual method recognizes the expenses in the period they are incurred and not in the period they are paid. **The expenses that have been incurred are to be reported during the year, although they have not been paid.**[4]

The claim of right doctrine is subsumed in the NIRC of 1997.

In the Motion for Reconsideration, respondent argues that that the claim of right doctrine is not applicable in the Philippines.[5] This argument must fail. The claim of right doctrine is in fact an offshoot of the general rule in recognition of income and deduction under the previously cited Sections 44 and 45 of the NIRC of 1997. Even more, the doctrine is not novel as it finds support in the basic accounting principle of accrual method.

When MERALCO unqualifiedly asserted its right over the provisional rate increase imposed upon its consumers and voluntarily reported the same as income, it is in effect recognizing the claim of right doctrine. In the claim of right doctrine, if a taxpayer receives money or other property and treats it as its own

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[4] Victorino C. Mamalateo, *Philippine Income Tax*, 2010 edition, pp. 335-336.
[5] *Rollo*, page 277.

under the claim of right that the payments are made absolutely and not contingently, such amounts are included in the taxpayer's income, even though the right to the income has not been perfected at that time. It does not matter that the taxpayer's title to the property is in dispute and that the property may later be recovered from the taxpayer.[6]

This doctrine was applied in several cases involving public utilities. In the case of *Brooklyn Union Gas Co. v. Comm., 62* F2d 505 (CCA2 1933),[7] a taxpayer, a utility company, in the course of rate dispute, had certain funds made available to it by an interlocutory order of court, subject to the taxpayer's posting of a security bond or securities of equal value. The taxpayer preferred not to take the funds on such conditions, and instead took them at the conclusion of litigation two years later. The taxpayer realized income in the earlier year under the claim-of-right rule, because the taxpayer had the power to secure the release of the funds, that is, there remained no effective restriction upon the taxpayer's dominion over them.[8]

Under this doctrine, if **the taxpayer who has included amounts in income pursuant to the claim-of-right doctrine subsequently repays those amounts, the taxpayer may be entitled to a deduction in the year**

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[6] Merten's *The Law of Federal Income Taxation*, Section 12A.145, Volume 2, (1995) citing Safety Tube Corp. v. Comm., 8 TC 757 (1947), affd 168 F2d 787 (CCA6 1948); Westover Co. v. Smyth, 43 AFTR 1283 (ND Cal 1951), citing Mertens text; Johns v. Comm., TC Memo 1956-119; Mensik v. Comm., 37 TC 703 (1962), affd 328 F2d 147 (CA7 1964); Marquardt Corp. v. Comm., 39 TC 443 (1962).
[7] As cited in Merten's *The Law of Federal Income Taxation*, Section 12A.152, Volume 2, (1995).
[8] *Ibid.*

of repayment.[9] However, to be entitled to a deduction, the taxpayer must meet the requirements of a statutory provision entitling him or her to a deduction.[10] For instance, it must qualify as a trade or business expense xxx,[11] or as a loss.[12]

In the case of *S. Lowenstein & Son, Inc. v. Comm.*, 21 TC 648, affd 222 F2d 919 (CA6 1955),[13] **it was ruled that the taxpayer's renunciation in a subsequent year of income received under claim of right does not defeat the earlier inclusion, but enables only the deduction in that subsequent year.**

Further, the United States Supreme Court in the case of *North American Oil Consolidated v. Burnet*, 286 U.S. 417 (1932),[14] (*North American* case) held that North American became entitled to the funds in 1917 under a claim of right, the year when it received funds subject of ongoing litigation NOT in the year 1922 when the case was finally resolved. Such rule gave substance to the annual accounting period as it afforded finality to the tax year by not holding it open until the eventual resolution of the dispute.[15]

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[9] *Supra*, note 1, Section 12A.146 citing Gaddis v. US., 330 F Supp 741 (D Miss 1971).
[10] *Supra*, note 1, Section 12A.146 citing E.g., IRC Section 162(a). See Grandview Mines v. Comm., 32 TC 759 (1959), affd 282 F2d 700 (CA9 1060); Berger v. Comm., 37 TC 1026 (1962). See also Equitable Life Ins. Co. of Iowa v. U.S., 340 F2d 9 (CA8 1965); National Life & Accident Ins. Co v. U.S., 244 F Supp 135 (MD Tenn 1965), citing Mertens text, affd 385 F2d 832 (CA6 1967) (deductions under life insurance companies' provisions of the Code).
[11] *Ibid.*, citing Oswald v. Comm., 49 TC 645 (1968).
[12] *Ibid.*, citing Comm. V. Switlik, 184 F2d 299 (CA3 1950); O'Meara v. Comm., 8 TC 622 (1947).
[13] As cited in Merten's *The Law of Federal Income Taxation*, Section 12A.161-162, Volume 2, (1995).
[14] Cited by Sanford M. Guerin and Philip F. Postlewaite, *Problems and Materials in Federal Income Taxation*, Fourth Edition, 1994, pages 824-826.
[15] *Ibid.*

The claim of right doctrine may be avoided if the taxpayer establishes its obligation to repay the amount received in the year of receipt and make provision for repayment. Establishment of a merely contingent obligation to repay will not suffice.[16] In this case, Meralco unconditionally recognized the overcharges as income from the time it filed its annual ITRs. It already claimed a right over an income knowing fully well the uncertainty and possible reversal of its case before the Supreme Court. When it took the risk of imposing higher rates to its consumers, it also assumed the risk of paying excess income taxes bearing in mind that the prescriptive period for refund disregards any supervening cause that may arise after payment. Consequently, the portion of the provisional increase subsequently rejected by the Supreme Court should have been considered as a deduction from income for taxable year 2003.

The claim of right doctrine was applied in our jurisprudence.

The local application of the claim of right doctrine was explained in the book *Philippine Income Tax* [17] citing the case of *Commissioner of Internal Revenue vs. Javier, Jr.*, (*Javier* case)[18] the pertinent portion of the discussion provides: gr

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[16] As cited in Merten's *The Law of Federal Income Taxation*, Section 12A.150, Volume 2, (1995) citing Nordberg v. Comm., 79 TC 655 (1982), affd 720 F2d 658 (CA1 1983), quoting Hope v. Comm., 55 TC 1020 (1971), affd 471 F2d 738 (CA3 1972), cert den 414 US 824 (1973).
[17] Victorino C. Mamalateo, 2010 edition, pages 79-80.
[18] G.R. No. 78953, July 31, 1991, 199 SCRA 824.

> ***3. Claim of right doctrine***. – A taxable gain is conditioned upon the presence of a claim of right to the alleged gain and the absence of a definite unconditional obligation to return or repay that which would otherwise constitute gain. To collect a tax would give the government an unjustified preference as to the part of the money that rightfully and completely belongs to the victim. The embezzlers title is void. (*Commissioner vs. Wilcox, 286 U.S. 417, 424*).
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> xxx Spouses Melchor and Victoria Javier filed their consolidated income tax return for the year with the notation "The taxpayer was the recipient of some money from abroad which he presumed to be a gift but turned out to be an 'error' and is now subject of litigation" but did not declare it as income. The court ruled that the amount received is income subject to tax, but the tax return filed cannot be considered as fraudulent because petitioner literally "laid his cards on the table" for respondent to examine. Error or mistake of fact or law is not fraud (*Commissioner vs. Javier, G.R. No. 71479, July 31, 1991, 199 SCRA 824*).
>
> ***Award of damages by lower court is taxable despite possibility of repayment in case judgment is reversed by appellate court.*** - If a taxpayer obtains earnings under a claim of right and without restriction as to its disposition, he has received income which he is required to include in his tax return, even though it may be claimed that he is not entitled to retain the money, and even though he may still be adjudged liable to restore its equivalent. Thus, where a taxpayer sued and was awarded damages by the trial court, and the award was received pending appeal, the money received is includible in his gross income, notwithstanding the possibility of repayment in case the judgment would be reversed by the appellate court (*North American Oil Consolidated vs. Burnett, 286 U.S. 417*).

In this case, the CTA ruled that gains are taxable in the year during which they are realized. This statutory policy is invoked in the interest of orderly administration. Collection of the revenue cannot be delayed, nor should the

Government be compelled to decide when a possessor's claims are without legal warrant.[19]

Hence, the amount credited to Javier, Jr. which he presumed to be a gift but turned out to be an error was subjected to tax. Thus, the claim of right doctrine is not new in this jurisdiction.

II. Claims for refund should be exercised within the prescriptive period fixed by law <u>regardless of any supervening cause</u> as emphatically provided under Section 229 of 1997 NIRC.

Even assuming, there is no other relief available to Meralco except to file a refund of its overpaid taxes, Section 229 of the NIRC of 1997 applies. However, the claim would still fail on account of prescription. Section 229 is emphatic on the requirement that the claim for refund must be filed within two (2) years from the date of payment in all cases in view of the phrase **"regardless of any supervening cause"**[20] that may arise after payment. The said provision categorically states:

> SEC. 229. *Recovery of Tax Erroneously or Illegally Collected.* — No suit or proceeding shall be maintained in any court for the recovery of any national

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[19] *Melchor J. Javier, Jr. vs. Ruben B. Ancheta, in his capacity as Commissioner of Internal Revenue* C.T.A. Case No. 3393, July 27, 1983, citing *Rutkin vs. United States*, 343 US 131, 137; 96 L. Ed. 835, 839 and *National City Bank vs. Helvering* [CA 2d] 98 F 2d 93, 96.

[20] Aban, Benjamin B., *Law of Basic Taxation in the Philippines*, revised edition, page 328.

> internal revenue tax hereafter alleged to have been erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority, or of any sum alleged to have been excessively or in any manner wrongfully collected until a claim for refund or credit has been duly filed with the Commissioner; but such suit or proceeding may be maintained, whether or not such tax, penalty, or sum has been paid under protest or duress.
>
> **In any case, no such suit or proceeding shall be filed after the expiration of two (2) years from the date of payment of the tax or penalty regardless of any supervening cause that may arise after payment:** Provided, however, That the Commissioner may, even without a written claim therefore, refund or credit any tax, where on the face of the return upon which payment was made, such payment appears clearly to have been erroneously paid. (emphasis ours)

This provision, which is, mandatory, is not subject to any qualification, and, hence, it applies regardless of the conditions under which the payment has been made.[21] Applying the above provision to the instant case, prescription has already set in, both in the administrative level (November 27, 2003) and judicial level (May 4, 2005) for the taxable years 1994-1998 and 2000. As expressly stated by law, the two (2)-year prescriptive period has already lapsed reckoned from the date of payment of the tax without consideration to any supervening cause that may arise after payment.

Section 229 of the NIRC of 1997 applies to overpayment of taxes.

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[21] *Guagua Electric Light Plant Co., Inc. vs. Collector of Internal Revenue*, G.R. No. 14421, April 29, 1961, 1 SCRA 1221, 1225.

Contrary to MERALCO's claim that Section 229 is limited only to erroneously and illegally paid taxes, existing jurisprudence will show that Section 229 applies even to overpaid taxes citing the cases of *Collector of Internal Revenue vs. Prieto* [22] and *Accra Investments Corporation vs. Court of Appeals*,[23] where the Supreme Court used the two (2)-year prescriptive period even when the issue involved was overpayment of taxes.

PD 69 added the phrase "regardless of any supervening cause."

The words of Section 229 clearly, plainly, and explicitly state that the two (2)-year prescriptive period is not affected by any supervening cause, hence, the phrase "***regardless of any supervening cause.***" This phrase was originally added by Presidential Decree No. 69 (PD 69) dated November 24, 1972 and was retained in both the 1977 and 1997 NIRC. The intent of the law is unmistakable, to establish as a condition *sine qua non* that all claims and actions for refund of any tax or penalty shall be filed within two years from the date of payment of such tax or penalty, "even if the taxpayer had no cause for refund as the tax or penalty, was legally collected, and **even if after the lapse of the two (2)-year period, a supervening cause should arise which would entitle the taxpayer to refund.**"[24]

[22] No. L-11976, August 29, 1961, 2 SCRA 1007.
[23] G.R. No. 96322, December 20, 1991, 204 SCRA 957.
[24] *Atlanta Land Corporation vs. Commissioner of Internal Revenue*, C.T.A. EB No. 79, May 23, 2006, C.T.A. Case No. 6987 citing Arañas, Annotations and Jurisprudence on the National Internal Revenue Code of 1977, As Amended, Sixth Edition, p. 571. Affirmed in G.R. No. 172773 dated June 18, 2007.

MERALCO's argument using the cases of *Commissioner of Internal Revenue vs. Insular Lumber Co.,*[25] (*Insular* doctrine) *Commissioner of Internal Revenue vs. National Power Corporation,* [26] and *Commissioner of Internal Revenue vs. Central Azucarera Don Pedro* is misplaced. These cases were promulgated ***before*** the addition of the phrase "***regardless of any supervening cause***." The then Tax Code did not specifically address the scenario where the tax was legally paid, but subsequently became erroneous upon the happening of a supervening cause. This brought about the *Insular* doctrine.

When PD 69 came in, it imposed a stricter rule on prescription. The only logical explanation for the addition of the phrase was to remedy the situation where the tax was legally collected but upon the occurrence of the supervening cause, the right to refund arises. Obviously, the *Insular* doctrine [reckoning the two (2)-year prescriptive period from the happening of the supervening cause] is no longer controlling and has long been abrogated by PD 69 with the inclusion of the phrase "***regardless of any supervening cause***."

As explained by former Commissioner of Internal Revenue Jose Arañas in his book entitled *Annotations and Jurisprudence on the National Internal Revenue Code of 1977,* [27] by this amendment, the old doctrine enunciated by the Supreme

[25] L-24221, December 11, 1967, 21 SCRA 1237.
[26] No. L-18874, January 30, 1970, 31 SCRA 112.
[27] Fourth edition, 1978, page 549.

Court in the *Insular* case no longer applies. This is the same conclusion reached by Associate Justice Japar B. Dimaampao in his book *Tax Principles and Remedies*[28] where he clarified that the ruling in *Insular* case is no longer in effect under the present law. The two (2)-year period is always to be reckoned from the date of the payment regardless of any supervening cause.[29]

Rationale behind the two (2) year prescriptive period.

The advent of the phrase "***regardless of any supervening cause***" espouses the rationale behind the two (2)-year prescriptive period which rests on the basic principles that "taxes are the lifeblood of the nation." A sound taxation requires that there is fiscal adequacy. The proceeds of tax revenue should coincide with, and approximate the needs of, government expenditures. *Neither an excess nor a deficiency of revenue vis-à-vis the needs of government would be in keeping with the principle.* [30]

In the case of *Atlanta Land Corporation vs. Commissioner of Internal Revenue* [31] the CTA *en banc* denied the claim for refund for being time-barred. The court disregarded the supervening causes such as the rescission of *dacion en pago* arrangement and subsequent enactment of RA 9182 or "The Special Purpose Vehicle Act" in reckoning the 2-year prescriptive period. The court

[28] Second edition, 2005, page 191.
[29] *Ibid.*
[30] Vitug and Acosta, *Tax Law and Jurisprudence*, Third Edition, page 2.
[31] *Supra*, note 24. Penned by Associate Justice Juanito C. Castañeda, Jr., with Presiding Justice Ernesto D. Acosta, Associate Justices Lovell R. Bautista, Erlinda P. Uy, Caesar A. Casanova, and Olga Palanca-Enriquez, concurring. Affirmed in G.R. No. 172773 dated June 18, 2007.

explained that the **availability of funds from the collection of taxes cannot forever be left subject to the contingency of refund brought about by certain acts which are solely within the exclusive control of the private contracting parties, otherwise, fiscal adequacy cannot be achieved.**[32] Without the strict observance of the prescriptive period, the government will always be at the losing end, refunding the taxes whenever supervening cause arises even after the expiration of the two (2)-year period and making the phrase "***regardless of any supervening cause***" futile and inoperative. In addition, claims for refund or tax credit should be exercised within the time fixed by law because the BIR being an administrative body enforced to collect taxes, its functions should not be unduly delayed or hampered by incidental matters.[33]

In the recent case of *United States vs. Clintwood Elkhorn Mining Co. et al.*,[34] (*Clintwood* case) US Supreme Court was unanimous in holding that the US Internal Revenue Code which provides for a two (2) and three (3)-year period of limitations in a claim for refund prevails over the longer period of limitations under the Tucker Act. In the said case, the taxpayers sought the refund of coal taxes which was later on ruled as unconstitutional. The US Supreme Court explained the rationale of the period of limitation in a claim for tax refund in this wise:

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[32] *Ibid.*

[33] *Philippine Bank of Communications vs. Commissioner of Internal Revenue,* G.R. No. 112024, January 28, 1999, 302 SCRA 241, 250.

[34] No. 07-308, April 15, 2008, 553 U.S. __ (2008), http://www.supremecourt.gov/opinions/07pdf/07-308.pdf

The Code further establishes a time limit for filing such a refund claim with the IRS: To receive a "refund of an overpayment of any tax imposed by this title in respect of which tax the taxpayer is required to file a return," a refund claim must be filed no later than "3 years from the time the return was filed or 2 years from the time the tax was paid, whichever of such period expires the later." §6511(a). And §6511(b)(1) mandates that "[n]o credit or refund shall be allowed or made" if a claim is not filed within the time limits set forth in §6511(a). "Read together, the import of these sections is clear: **unless a claim for refund of a tax has been filed within the time limits imposed by §6511(a), a suit for refund... may not be maintained in any court**." *Dalm, supra*, at 602.

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Indeed, we all but decided the question presented over six decades ago in United States v. A.S. Kreider Co., 313 U.S. 443 (1941). Section 1113(a) of the Revenue Act of 1926, like the refund claim provision in §7422(a) of the current Code, prescribed that "[n]o suit or proceeding shall be maintained in any court for the recovery of any internal-revenue tax alleged to have been erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority, or of any sum alleged to have been excessive or in any manner wrongfully collected until a claim for refund or credit has been duly filed with the Commissioner of Internal Revenue," and established a time limit for bringing suit once the claim-filing requirement had been met. 44 Stat. 116. Like the companies here, A.S. Kreider had failed to file a tax-refund action within that limitations period. See 313 U.S., at 446. And, like the companies here, A.S. Kreider argued that it was instead subject only to the longer 6-year statute of limitations under the Tucker Act. *Id.*, at 447.

We rejected the claim, holding that the Tucker Act limitations period "was intended merely to place an outside limit on the period within which all suits must be initiated" under that Act, and that "Congress left it open to provide less liberally for particular actions which, because of special considerations, required different treatment." *Ibid.* **We held that the limitations period in §1113(a) was "precisely that type of provision," finding that Congress created a shorter statute of limitations for**

> **tax claims because "suits against the United States for the recovery of taxes impede effective administration of the revenue laws. *Ibid.* If such suits were allowed to be brought subject only to the 6-year limitations period in the Tucker Act, we explained, §1113(a) would have "no meaning whatever."** *Id.*, at 448. So too here. The refund scheme in the current Code would have "no meaning whatever" if taxpayers failing to comply with it were nonetheless allowed to bring suit subject only to the Tucker Act's longer time bar.
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>
> In any event, we see no constitutional problem at all. Congress has indeed established a detailed refund scheme that subjects complaining taxpayers to various requirements before they can bring suit. This scheme is designed "**to advise the appropriate officials of the demands or claims intended to be asserted, so as to insure an orderly administration of the revenue,**" *United States v. Felt & Tarrant Mfg. Co.*, 283 U.S. 269, 272 (1931), **to provide that refund claims are made promptly, and to allow the IRS to avoid unnecessary litigation by correcting conceded errors. Even when the constitutionality of a tax is challenged, taxing authorities do in fact have an "exceedingly strong interest in financial stability,**" *McKesson Corp. v. Division of Alcoholic Beverages and Tobacco, Fla. Dept. of Business Regulation,* 496 U.S. 18, 37 (1990), **an interest they may pursue through provisions of the sort at issue here.**[35] (emphasis ours)
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> xxx xxx xxx

It is to be noted that the US Supreme Court strictly applied the period of limitation under its tax code despite the constitutional nature of the taxpayer's claim. The taxpayer succumbed to an unconstitutional tax, and sought recourse only after it has been unlawfully exacted.[36] Nonetheless, the US Supreme Court

[35] *Supra* note 34.
[36] *Supra* note 34.

rejected the claim for failure to comply with the refund scheme and for being time-barred. It ruled that unconstitutional taxation claim is also subject to prescriptive period just as any other claim can, it says:

> The outcome here is clear given the language of the pertinent provisions. Title 26 U.S.C. §7422(a) states that "[n]o suit... shall be maintained in any court for the recovery of any internal revenue tax alleged to have been erroneously or illegally assessed or collected, or any penalty claimed to have been collected without authority, or of any sum alleged to have been excessive or in any manner wrongfully collected, until a claim for refund... has been duly filed with" the IRS. (Emphasis added.) Here the companies did not file a refund claim with the IRS for the 1994-1996 taxes, and therefore may bring "[n]o suit" in "any court" to recover "any internal revenue tax" or "any sum" alleged to have been wrongfully collected "in any manner." Five "any's" in one sentence and it begins to seem that Congress meant the statute to have expansive reach.
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> Moreover, the time limits for filing administrative refund claims in §6511-set forth in an "unusually emphatic form," United States v. Brockamp, 519 U.S. 347, 350 (1997)-apply to "any tax imposed by this title," 26 U.S.C. §6511(a) (emphasis added). **The statute further provides that "[n]o credit or refund shall be allowed or made after the expiration of the period of limitation prescribed subsection (a)... unless a claim for credit or refund is filed by the taxpayer within such period."** §6511(b)(1). Again, this language on its face plainly covers the companies' claim for a "refund" of "tax[es] imposed by" Title 26, specifically 26 U.S.C. §4121. The companies argue that these statutory provisions are ambiguous, Brief for Respondents 43-45, but we cannot imagine what language could more clearly state that taxpayers seeking refunds of unlawfully assessed taxes must comply with the Code's refund scheme before bringing suit, including the requirement to file a timely administrative claim.
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> xxx xxx xxx
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> The companies do not argue for such an exemption simply because their claims are based on a constitutional violation. As they acknowledge, *id.*, at 34, a

> **"constitutional claim can become time barred just as any other claim can,"** *Block v. North Dakota ex rel. Board of Univ. and School Lands*, 461 U.S. 273, 292 (1983). xxx (emphasis ours)
>
> xxx We see no reason why compliance with straightforward administrative requirements and reasonable time limits to seek a refund once a tax has been paid should lead to a different result.[37]
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> xxx xxx xxx

Thus, in a claim for refund, a taxpayer must prove not only his entitlement to a refund but also his compliance with the procedural due process as non-observance of the prescriptive periods within which to file the administrative and the judicial claims would result in the denial of his claim. [38]

American cases have persuasive effect in our jurisdiction.

Jurisprudence is replete with cases reiterating the position that our income tax laws being of American origin, interpretations by the American courts of our parallel tax laws have persuasive effect on the interpretation of these laws.[39] Having said this, the cited cases of *Clintwood, North American* and *Brooklyn* would show the final termination of the litigation was NOT considered to be relevant or critical in determining the period to file refund in case of overpayment or in determining the period to recognize income. If at all, termination of the

[37] *Supra* note 34.
[38] *Commissioner of Internal Revenue v. Aichi Forging Company of Asia, Inc.*, G.R. No. 184823, October 6, 2010, 632 SCRA 422.
[39] *Chamber of Real Estate and Builders' Association, Inc. vs. Romulo*, G.R. No. 160756, March 9, 2010, 614 SCRA 605, *Commissioner of Internal Revenue vs. Solidbank Corporation*, G.R. No. 148191, November 25, 2003, 416 SCRA 436, 453, *Commissioner of Internal Revenue vs. Citytrust Investment Phils., Inc.*, G.R. Nos. 139786 & 140857, September 27, 2006, 503 SCRA 398, *Philippine Health Care Providers, Inc. vs. Commissioner of Internal Revenue*, G.R. No. 167330, September 18, 2009, 600 SCRA 413.

litigation merely determined whether or not there is right to retain income already received. Thus, the final and executory Decision of the Supreme Court in MERALCO's case is not the reckoning point of the two (2)-year prescriptive period but merely gives rise to its obligation to repay its customers with the eventuality that it can deduct the repayments from the income in the year incurred.

III. Meralco failed to discharge the burden of proving its entitlement to tax refunds.

Tax refunds are in the nature of tax exemptions. As such, they are regarded as in derogation of sovereign authority and to be construed *strictissimi juris* against the person or entity claiming the exemption. [40] Thus, the burden of proof is upon him who claims the exemption in his favor and he must be able to justify his claim by the clearest grant of organic or statute law and cannot be permitted to exist upon vague implications.[41] Since tax refunds partake of the nature of tax exemptions, which are construed *strictissimi juris* against the taxpayer, evidence in support of a claim must likewise be *strictissimi* scrutinized and duly proven.[42]

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[40] *Commissioner of Internal Revenue vs. S.C. Johnson and Son, Inc.*, G.R. No. 127105, June 25, 1999, 309 SCRA 87, 108 citing *Commissioner of Internal Revenue vs. Tokyo Shipping Co., Ltd.*, 244 SCRA 332; *Province of Tarlac vs. Alcantara*, 216 SCRA 790, *Magsaysay Lines, Inc. vs. Court of Appeals*, 260 SCRA 513.

[41] *Ibid.*

[42] *Commissioner of Internal Revenue vs. Far East Bank & Trust Co.* (now BPI), G.R. No. 173854, March 15, 2010, 615 SCRA 417, 431 citing *Atlas Consolidated Mining and Development Corporation v. Commissioner of Internal Revenue*, G.R. No. 159490, February 18, 2008, 546 SCRA 150, 163.

Refund cannot be made to depend upon a condition.

Assuming without conceding, MERALCO's claim has not yet prescribed, the claim is at best premature and would still fail with respect to the overcharges not yet refunded to petitioner's consumers. The granting of refund cannot be made to depend upon the happening of a condition or a contingency. The amount to be refunded has not yet been fully returned to its consumers. In Meralco's Notes to Financial Statements[43] for the year ended December 31, 2007, assuming the previous payments were indeed repaid, there remained an estimated balance of P14,396M not yet refunded.

The claim was not duly proven.

Moreso, the refund is subject to a condition that the overcharges should have been actually given or credited to future consumption of Meralco's consumers. Meralco admitted that some of the electric service accounts of its consumers entitled to refund are terminated, hence, it acceded to the probability that the entire gross refund amount of P30,230,092,522.39 may not be fully refunded or credited to future consumption.[44] This only shows that the instant case would still fail due to insufficiency of evidence to determine whether the total amount was actually repaid to Meralco's consumers.

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[43] Respondent's Formal Offer of Evidence, Exhibit "PPP"
[44] Respondent's Motion for Partial Reconsideration and Clarification, Division docket p. 1259.

The determination of the amount repaid is necessary in granting this tax refund, otherwise, the government would be in a position of refunding an income tax, the tax base of which is still within the coffers of Meralco and may or may not be repaid to its consumers. Until and unless repayment can be ascertained, Meralco's overcharges are still considered income under the claim of right doctrine, thus, the claim for refund under this situation must fail.

Submission of evidence at this stage of the proceeding is not proper.

MERALCO is no longer entitled to submit forgotten evidence to prove its entitlement to refund considering that the case is already pending before the CTA *en banc.* To remand the case to the CTA Second Division for reception of evidence is a violation of Rule 37 of the Rules of Court. A new trial may only be granted when there is fraud, accident, mistake, excusable negligence or there is newly discovered evidence. Rule 37 provides:

> RULE 37
> NEW TRIAL OR RECONSIDERATION
>
> Section 1. *Grounds of and period for filing motion for new trial or reconsideration.* - Within the period for taking an appeal, the aggrieved party may move the trial court to set aside the judgment or final order and grant a new trial for one or more of the following causes materially affecting the substantial rights of said party:
>
> > (a) Fraud, accident, mistake or excusable negligence which ordinary prudence could not have guarded against and by reason of which such aggrieved party has probably been impaired in his rights; or

> (b) Newly discovered evidence, which he could not, with reasonable diligence, have discovered and produced at the trial, and which if presented would probably alter the result.
>
> Within the same period, the aggrieved party may also move for reconsideration upon the grounds that the damages awarded are excessive, that the evidence is insufficient to justify the decision or final order, or that the decision or final order is contrary to law.

None of the grounds mentioned above is present in this case. Hence, it is too late for MERALCO to prove its case at this stage of the proceeding.

Conclusion

The first duty of the court is to apply the law where the terms of the statute are clear and unambiguous.[45] Regardless of our reservations as to the wisdom or the perceived ill-effects of a particular legislative enactment, the court is without authority to modify the same as it is the exclusive province of the law-making body to do so.[46] Sections 44 and 45 of the NIRC of 1997 dictate that MERALCO's overcharges to be repaid to its customers, previously reported as income, should have been claimed as deductible expense at the time when the obligation to repay arises, i.e. on May 5, 2003 when the Decision of the Supreme Court attained finality. This is in recognition of the claim of right doctrine consistent with the accrual method of accounting used by MERALCO. Assuming arguendo we apply Section 229 of the NIRC of 1997, the claim would still fail due

[45] *City Government of Tagaytay vs. Guerrero,* G.R. Nos. 140743 & 140745; 141451-52. September 17, 2009, 600 SCRA 33.

[46] *Gulf Air Company, Philippine Branch (GF) vs. Commissioner of Internal Revenue*, G.R. No. 182045, September 19, 2012.

to the stringent character of the phrase "regardless of any supervening cause." Even if the period has not yet prescribed, the claim was not duly proven, at best premature with respect to overcharges not yet refunded to customers. Thus, the claim for refund under this situation must fail.

In light of the foregoing, MERALCO's "Motion for Reconsideration" should be DENIED.

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

REPUBLIC OF THE PHILIPPINES
Court of Tax Appeals
QUEZON CITY

EN BANC

COMMISSIONER OF INTERNAL REVENUE, *Petitioner,*	**C.T.A. EB NO. 773** **(C.T.A. CASE NO. 7242)**
	Present:
-versus-	ACOSTA, Presiding Justice, CASTAÑEDA, JR., BAUTISTA, UY, CASANOVA, PALANCA-ENRIQUEZ, FABON-VICTORINO, MINDARO-GRULLA, and COTANGCO-MANALASTAS, JJ.
MANILA ELECTRIC COMPANY, INC., *Respondent.*	**Promulgated:** NOV 13 2012 2:15 p.m.

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SEPARATE DISSENTING OPINION

PALANCA-ENRIQUEZ, J.:

With all due respect to the majority, I join the Dissenting Opinion of my esteemed colleague, Justice Juanito C. Castañeda, Jr.. However, if only to fortify my stand that our Decision dated May 8, 2012 in the above-captioned case be maintained, I would like to expound on the following points.

At the outset, I would like to emphasize that after carefully considering the grounds raised in respondent MERALCO's Motion for Reconsideration, I find that the grounds and arguments raised therein have already been amply discussed and passed upon in our Decision dated May 8, 2012. The additional arguments stated therein constitute neither compelling nor cogent reason to modify, much less reverse our Decision dated May 8, 2012.

The majority finds partial merit in respondent MERALCO's Motion for Reconsideration on the ground that the two-year prescriptive period under *Section 229 of the NIRC of 1997* may be suspended for reasons of equity and other special circumstances, citing the case of *Commissioner of Internal Revenue vs. Philippine American Life Insurance Co., G.R. No. 105208, May 29, 1995 ("Philam case").*

Equity Applies Only in the Absence of, But Never Against a Statutory Law or Rules of Procedure

However, well settled is the rule that equity may not be applied in the presence of a statutory law or judicial rules of procedure. Our courts are basically courts of law and not courts of equity (*Agra, et al. vs. Philippine*

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National Bank, G.R. No. 133317 June 29, 1999). In the case of *Arsenal v. Intermediate Appellate Court, 143 SCRA 40,* the Supreme Court ruled that it is a long standing principle that equity follows the law. Courts exercising equity jurisdiction are bound by rules of law and have no arbitrary discretion to disregard them.

Thus, in the case of *Zabat, Jr. v. Court of Appeals, 142 SCRA 587*, the Supreme Court was more emphatic in upholding the rules of procedure, as follows:

> "As for equity, which has been aptly described as a 'justice outside legality,' this is applied only in the absence of, and never against, statutory law or, as in this case, judicial rules of procedure. *Aequetas nunguam contravenit legis.* The pertinent positive rules being present here, they should pre-empt and prevail over all abstract arguments based only on equity."

In the present case, *Section 229 of the NIRC of 1997, as amended*, is clear and categorical in providing a prescriptive period to claim for refund of any national internal revenue tax hereafter alleged to have been erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority, or of any sum alleged to have been excessively or in any manner wrongfully collected, to wit:

> "**SEC. 229. Recovery of Tax Erroneously or Illegally Collected** – No suit or proceeding shall be maintained in any court for the recovery of any national internal revenue tax hereafter alleged to have been erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority, or of any sum alleged to have been excessively or in any manner wrongfully collected, until a claim for refund or credit has been duly filed with the Commissioner; but such suit or proceeding may be maintained, whether or not such tax, penalty, or sum has been paid under protest or duress.
>
> In any case, no such suit or proceeding shall be filed after the expiration of two (2) years from the date of payment of the tax or penalty regardless of any supervening cause that may arise after payment: Provided, however, That the Commissioner may, even without a written claim therefor, refund or credit any tax, where on the face of the return upon which payment was made, such payment appears clearly to have been erroneously paid".

Corollary thereto, the *2005 Revised Rules of the CTA, as amended*, specifically the last sentence of *Section 3(a)(2) of Rule 4* thereof, provides that in the case of claims for refund of taxes erroneously or illegally collected, the taxpayer must file a petition for review with this Court in

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Division prior to the expiration of the two (2)-year period under *Section 229 of the NIRC of 1997*, to wit:

> "SEC. 3. Cases within the jurisdiction of the Court in Division. – The Court in Division shall exercise:
>
> (a) Exclusive original over or appellate jurisdiction to review by appeal the following:
>
> (2) xxx Provided, still further, that in the case of claims for refund of taxes erroneously or illegally collected, the taxpayer must file a petition for review with the Court prior to the expiration of the two-year period under Section 229 of the National Internal Revenue Code;
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> xxx xxx"

Hence, considering the above express provisions of the law providing a prescriptive period to file claims for refund of erroneously, illegally, excessively or wrongfully collected taxes, equity will not apply here; otherwise, it would be tantamount to overruling or supplanting the express provisions of the law.

<u>Philam Case is not on All Fours with the Instant Case</u>

Likewise, I cannot agree in the majority's reliance on the *Philam case* as the *Philam case* is not on all fours with the instant case. The issue involved in the *Philam case* was the reckoning of the two (2)-year prescriptive period for the recovery of taxes when the law requires the filing of a final adjustment return on a specified date after the end of the taxable year. In that case, taking into consideration the statutory requirement to file a final adjustment return, both the administrative and judicial claims for refund were filed within the two (2)-year prescriptive period. Furthermore, the cases cited in *Philam case,* such as *Oral & Dental College vs. Court of Tax Appeals, 102 Phil 912 and Panay Electric Co., Inc. vs. Collector of Internal Revenue and Court of Appeals, 103 Phil 819*, are also not applicable in this case. In said cases, the taxpayers paid the taxes in faithful compliance of the law and without assuming any risk resulting from their actions.

On the other hand, in the present case, the crux of the controversy is whether or not MERALCO is entitled to a claim for refund of its overpaid taxes for taxable years 1994 to 1998 and 2000. Moreover, MERALCO's administrative claim for refund filed on November 27, 2003 and judicial claim for refund filed on May 4, 2005 were both filed way beyond the two (2)-year prescriptive period. Also, here, MERALCO took the risk of imposing higher rates to its consumers, notwithstanding that the rate increase granted by the Energy Regulatory Board was merely provisional and subject to a condition that after hearing and evaluation, should MERALCO be entitled to a lesser increase rate, all excess collected by it shall be refunded to its customers or credited to future consumption. When MERALCO took the risk of imposing higher rate to its customers, it also assumed the risk of paying excess income taxes. Having assumed that risk, MERALCO should have been more vigilant and circumspect in observing the prescriptive period as regards its excess income taxes.

Thus, considering the foregoing, the suspension of the two-year prescriptive period in the Philam case for reasons of equity and other special circumstances cannot be applied in this case.

Section 229 is Explicit in Providing that the date of Payment of the Tax is the Reckoning Point of the Two-Year Prescriptive Period and does not Provide for Any Suspension of the Running of the Two-Year Prescriptive Period

The majority rules that while *Section 229* is mandatory, the prescriptive period has not commenced to run as the same was suspended due to special circumstances obtaining in this case. To that, I cannot agree.

Section 229 is explicit in providing that the claim for refund should be filed within two (2) years from the date of payment of the tax, regardless of any supervening cause that may arise after payment. The statute does not provide for any suspension of the running of the two (2)-year prescriptive period. Section 229 expressly provides that no suit or proceeding for the recovery of any national internal revenue tax erroneously or illegally collected shall be filed after the expiration of two (2) years from the date of payment of the tax regardless of any supervening cause that may arise after payment.

Therefore, with the inclusion in Section 229 of the phrase "regardless of any supervening cause that may arise after payment", by PD 69, and said phrase having been carried over both in the *1977 Tax Code* and the *NIRC of 1997, as amended*, the intention of the lawmakers

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is to provide a condition *sine qua non* that all claims for refund of erroneously, illegally, excessively or wrongfully collected taxes or penalty shall be filed within two (2) years from the date of payment of the tax. Evidently, the doctrine enunciated in the case of *Commissioner of Internal Revenue vs. Insular Lumber Co., L-24221, December 11, 1967* ("Insular doctrine") reckoning the two (2)-year prescriptive period from the happening of the supervening cause is no longer controlling and had long been abrogated by PD 69 when it included the phrase "regardless of any supervening cause". Hence, MERALCO's invocation of the Insular doctrine is misplaced. Likewise, MERALCO's reliance on the case of *Commissioner of Internal Revenue vs. National Power Corporation, No. L-188874, January 30, 1970*, having been promulgated before the inclusion in Section 229 of the phrase "regardless of any supervening cause" by PD 69, which took effect on November 27, 1972, is also misplaced.

It can be inferred from the majority's opinion that the special circumstances in the present case justifying the suspension of the reckoning of the two (2)-year prescriptive period are the following facts:

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that on December 23, 1993, respondent MERALCO filed with the ERB an application for revised rates with an average increase of P0.21 per kilo watt hour ("kwh") in its distribution charge; on January 28, 1994, the ERB granted a provisional increase of P0.184 per kwh, subject to the condition that in the event the ERB determines that respondent is entitled to a lesser increase in rates, all excess amounts collected by respondent shall be refunded to its customers or credited in their favor; thus, MERALCO paid the income tax due on its taxable income based on gross electric revenue computed at an average basic distribution rate of P2.996 per kwh (i.e., existing average rate of P2.812 per kwh, plus provisional increase of P0.184); however, on February 16, 1998, the ERB, adopting the recommendations of the COA, rendered a Decision granting a rate increase of only P0.17 per kwh and ordered MERALCO to refund or credit to its customers the average amount of P0.167 per kwh beginning February 1994; but, instead of following the ERB's order, MERALCO appealed the decision of the ERB to the Court of Appeals, which rendered a decision on February 24, 1999 reversing the ERB decision; as a consequence, the CIR and the Lawyers Against Monopoly and Poverty, et al. appealed the decision of the Court of Appeals to the Supreme Court; on November 15, 2002, the Supreme Court rendered a decision reversing the decision of the Court of Appeals and affirming the ERB decision dated February 16, 1998; and said decision of the Supreme Court became final and executory on May 5, 2003.

From the foregoing factual circumstances that transpired in the present case, it is clear that the amount being claimed for refund by MERALCO basically arose because MERALCO filed with the ERB an application for revised rates. It was not brought about by reason of a statutory provision, but on account of MERALCO's own volition. In applying for a revised rate, MERALCO took the risk that its application may be granted or denied. When the ERB provisionally granted and subjected to a condition its application for increase, MERALCO should have known the consequences of a possible reduction or denial of its claim. By the time MERALCO received a copy of the Decision dated February 16, 1998 of the ERB, it already knew that it had overcharged its customers by P0.167 per kwh and that it had to refund its customers said overcharge beginning February 1994, as ordered by the ERB.

Thus, it cannot be said that it was only on May 5, 2003 that MERALCO had ascertained that its income tax payment for taxable years 1994 to 1998 and 2000 had become erroneous. As early as February 16, 1998, when MERALCO received the Decision of the ERB ordering it to refund its consumers the overcharge of P0.167 per kwh, MERALCO knew that it has excessively paid its taxes for taxable years 1994 to 1998.

Considering that *Section 229* does not only apply to erroneously or illegally paid taxes, but also to excessively or overpaid taxes, then I cannot agree with the majority's view that the two (2)-year prescriptive period should commence to run only from May 5, 2003, the date the decision of the Supreme Court had become final and executory, when MERALCO allegedly claims that its income payments for taxable years 1994 to 1998 and 2000 had become erroneous. Prior to the finality of the Supreme Court Decision on May 5, 2003, when the ERB, in its decision dated February 16, 1998, ordered MERALCO to refund or credit to its customers the average amount of P0.167 per kwh beginning February 1994, MERALCO knew that it has overpaid its taxes for taxable years 1994 to 1998. Knowing fully-well the two-year prescriptive period for claims for refund of erroneously, illegally, excessively or wrongfully collected taxes provided in *Section 229*, then MERALCO should have filed its claim for refund within said period in order that its claim should not have prescribed.

Records, however, show that MERALCO filed its administrative claim for refund on November 27, 2003 and its judicial claim for refund on May 4, 2005, which are clearly, way beyond the two (2)-year prescriptive period.

Solutio Indebiti does not Apply in the Instant Case

The majority rules that the principle of *solutio indebiti* is applicable for refunds of erroneously or illegally collected or assessed taxes.

Though, I agree with the majority that in certain instances, the principle of *solutio indebiti* is applicable to refunds of erroneously or illegally collected taxes, if the requisites of *solutio indebiti* are complied with; however, the prescribed elements for the applicability of *solutio indebiti,* which are:

(1) a payment is made when there exists no binding relation between the payor, who has no duty to pay, and the person who received the payment; and

(2) the payment is made through mistake, and not through liberality or some other cause *(Siga-an vs. Villanueva, 576 SCRA 708)*,

are wanting in the present case.

As regards the first element, there exists a binding relation between MERALCO and the CIR. MERALCO is a taxpayer obligated to pay income taxes on the income it declared in its income tax returns for the years 1994 to 1998 and 2000. Since MERALCO recognized as income the provisional increase of rate granted by the ERB, notwithstanding that the increase granted was merely conditional, then, it has the obligation to pay the income taxes due thereon.

As regards the second element, there was no mistake on the part of MERALCO when it paid the income taxes to the BIR for the years 1994 to 1998 and 2000. MERALCO was fully aware of the status of its application for revision of its rate schedule and the proceedings that transpired thereafter. It was fully aware that the increase granted to it in the ERB Order dated January 28, 1994 was merely provisional and subject to the condition that after hearing and evaluation, should MERALCO be entitled to a lesser increase in rates, all excess collected by MERALCO shall be refunded to its customers or credited to their future consumption. At the outset, when the ERB provisionally granted and subjected to a condition its application for increase, MERALCO should have known the consequences of a possible reduction of its application.

For all of the foregoing, I maintain my original stand that MERALCO's administrative claim for refund filed on November 27, 2003 and judicial claim for refund filed on May 4, 2005 were both filed way beyond the two(2)-year prescriptive period. I, therefore, vote to

DENY respondent MERALCO's "Motion for Reconsideration" for lack of merit.

OLGA PALANCA-ENRIQUEZ
Associate Justice