REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

ARMCO-MARSTEEL ALLOY CORPORATION,
Petitioner,

- versus -

C.T.A. CASE NO. 4592

THE COMMISSIONER OF INTERNAL REVENUE,
Respondent.

7/1/93

x - x

DECISION

This case involves petitioner's claim for refund or in the alternative tax credit of alleged overpaid income tax for the fiscal year ending October 31, 1989 in the amount of P5,061,899.00.

Petitioner is a domestic corporation registered with the Board of Investments as a preferred pioneer enterprise engaged in the business of producing/manufacturing grinding balls and billets. (#11, Notes to Financial Statements, p. 53, CTA record.) Petitioner is entitled to avail as an incentive under R.A. 5186 the allowable deductions of the accelerated depreciation. (BIR Form 1702-E, p. 73, CTA record.)

Petitioner's annual income tax return for the fiscal year ending October 31, 1989 was filed on February 15, 1990. The income tax return shows a refundable amount of P5,061,899.00, computed as follows:

Total Gross Income				P71,764,226.00
Less: Total Deductions				66,807,558.00
Net Income				P 4,956,668.00
Amount of Tax Due				P 1,734,834.00
Less: Quarterly Tax Payments				
Quarter	OR Number	Date Paid	Amount	
First	B14210875	03-31-89	P4,583,182.00	
Second	B17039220	06-29-89	2,213,551.00	6,796,733.00
Total Amount of Tax Refundable				P 5,061,899.00

For the succeeding taxable fiscal year ending October 31, 1990, petitioner suffered a loss. Thus, petitioner was not able to apply the refundable amount as an automatic tax credit pursuant to the provision of Section 69 of the National Internal Revenue Code.

On February 21, 1991, petitioner filed a claim for refund in the amount of P5,061,899.00 citing as basis Section 69 of the said Code, to wit:

> "**Sec. 69. Final Adjustment Return** - Every corporation liable to tax under Section 24 shall file a final adjustment return covering the total taxable income for the preceding calendar or fiscal year. If the sum of the quarterly tax payments made during the said taxable year is not equal to the total tax due on the entire taxable income of that year the corporation shall either:
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> a) Pay the excess tax still due; or

> b) Be refunded the excess amount paid, as the case may be.
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> In case the corporation is entitled to a refund of the excess estimated quarterly income taxes paid, the refundable amount shown on its final adjustment return may be credited against the estimated quarterly income tax liabilities for the taxable quarters of the succeeding taxable year."

To date, respondent has not acted on the claim for refund/tax credit filed by petitioner. Hence, on April 3, 1991, petitioner filed the instant petition for review.

Respondent answered that the petition states no cause of action for failure on the part of petitioner to allege the date/s when the quarterly income tax payments were made. In addition, all payments made prior to April 3, 1989 have prescribed. The quoted provision (Section 69) is misplaced. It is incumbent upon the taxpayer to prove entitlement to the refund/credit sought.

The issue is simple. Is petitioner entitled to the refund or tax credit of P5,061,899.00, representing overpaid income tax for the fiscal year ending October 31, 1989?

The Court answers in the affirmative.

During the trial of this case, petitioner offered in evidence the following documents:

1. Quarterly Income Tax Returns ending:

a. January 31, 1989 (Exh. A) with a tax due of P4,583,182.00 (Exh. A-2);

b. April 30, 1989 (Exh. B) with a tax due of P2,213,551.00 (Exh. B-2); and

c. July 31, 1989 (Exh. C) with a refundable amount of of P2,006,808.00 (Exh. C-2).

2. Annual Income Tax Returns, with the attached Auditor's Report and Financial Statements, for the fiscal years ending:

a. October 31, 1989 (Exh. D-1) showing an Income Tax Due of P1,734,834.00 and Income Tax Refundable amount of P5,061,899.00 (Exh. D-2); and

b. October 31, 1990 (Exh. F) showing a loss of P11,984,215.00 thereby indicating no tax liability (Exh. F-1).

3. Quarterly Income Tax Payments for the first and second quarters of fiscal year 1989, consisting of:

a. BIR Payment Order No. C4899806 (Exh. A-3) and CB Confirmation Receipt No. B14210876 (Exh. A-5) both dated March 31, 1989 (Exhs. A-4 and A-6, respectively) in the amount of P4,583,182.00, representing income tax paid for the first quarter of 1989; and

b. BIR Payment Order No. C5436681 (Exh. B-3) and CB Confirmation Receipt No. B17039220 (Exh. B-5) both dated June 29, 1989 (Exhs. B-4 and B-6, respectively) in the amount of P2,213,551.00, representing income tax paid for the second quarter of 1989.

4. The letter claim for refund (Exh. G) dated February 20, 1991 filed by petitioner with respondent's office on February 21, 1991 (Exh. G-1).

Respondent for his part presented as witness, Mrs. Jane Denosta, Revenue Officer II, BIR, Makati East District, one of the revenue examiners who conducted the examination on petitioner's alleged claim for refund. The Statement of Findings (Exh. 1) shows that instead of a refund petitioner was found to be liable for deficiency income tax in the amount of P5,333,742.34, computed as follows:

I. INCOME :

Net income per return	P 4,956,668.00
Add: Unallowable accelerated depreciation	6,176,375.00
Repair and Maintenance expense charge to expense that should be capitalized	2,413,193.17
Adjusted net income	P13,546,236.17
Income tax due	P 4,741,182.66
Less: Income tax per return	1,734,834.00
Income Tax still due	P 3,006,348.66
Add: 25% surcharge	751,587.16
20% Interest 2 yrs. & 1 mo. 41.6665%	1,565,806.52
Compromise penalty	10,000.00
Total Deficiency Income Tax	P 5,333,742.34

Repair and Maintenance Schedule

40404	JV-7-24	803 Spare parts GJ 65-0042	P 369,249.28
40404	JV-6-14	Rep/Main GJ 57-0009	287,000.00
40404	JV-9-25	Landed Cost GJ-86-0016	207,908.12
87093	Cuyos March 113 Pinion gear		249,136.36
40404	JV-8-14	Rep. and Maintenance	264,530.00
40404	JV-4-21	SMD-Raw material	280,100.00
82225	Bearing	Roller Bearing PJTO-0079	349,090.01
82277	ABB	818 Transformer PJ04-0040	150,000.00
40404	JV-1-26	Landed cost 903 GJ03-0065	256,178.50
			P 2,413,139.19

Respondent's revenue examiner testified that upon investigation petitioner was not able to secure the approval of the BIR regarding the use of the accelerated method of depreciation. Thus, the disallowance of P6,176,375.00 accelerated depreciation.

Likewise, the amount of P2,413,139.19, representing some of the repairs and maintenance expense, was disallowed on the ground that the same should have been capitalized because of its material amount as compared to others with minimal amounts.

At this juncture it may be noteworthy to point that petitioner requested the BIR for the privilege to use the accelerated depreciation method. But up to hearing date the same was not acted upon by respondent's office. Also, nowhere in the records of the case will it show that the 10-day preliminary notice of assessment was sent to petitioner.

We shall first discuss each items raised by respondent in his answer to the petition.

Respondent contended that the petition states no cause of action there being no mention of the dates when the taxes were paid. Furthermore, payments made after April 3, 1989 have already prescribed.

In an earlier ruling of the Supreme Court in the case of **Commissioner of Internal Revenue v. Asia Australia Express Ltd., G. R. No. 85956, April 10, 1989,** it was held that "where the tax is payable by the taxpayer in quarterly installments, the final payment is the last quarter payment at the end of the tax year when it is finally ascertainable that the taxpayer either made profits or suffered losses in its operations".

In the subsequent case of **Commissioner of Internal Revenue v. TMX Sales, Inc., et. al. G.R. No. 83736, January 15, 1992,** the Supreme Court ruled that "the most reasonable and logical application of the law would be to compute the two-year prescriptive period at the time of filing the Final Adjustment Return or the Annual Income Tax Return, when it can be finally ascertained if the taxpayer has still to pay additional income tax or if he is entitled to a refund of overpaid income tax."

In the case at bar, the corporate quarterly and annual income tax return for the fiscal year ending October 31, 1989 as well as the confirmation receipts and payment orders showing the amount of taxes paid, were all attached to the petition. If examined closely the annexes of the petition clearly shows the date when said taxes in questioned were paid. The petition, therefore, states a cause of action.

The quarterly income tax payments for the first and second quarters of fiscal year 1989 should only be considered mere instalments of the annual tax due. "These quarterly tax payments which are computed based on the cumulative figures of gross receipts and deductions in order to arrive at a net taxable income, should be treated as advances or portions of the annual income tax due, to be adjusted at the end of the calendar or fiscal year. This is reinforced by Section 87 (now Section 69) which provides for the filing of adjustment returns and final payment of income tax. Consequently, the two-year prescriptive period provided in Section 292 (now Section 230 of the Tax Code should be computed from the time of filing the Adjustment Return or Annual Income Tax Return and final payment of income tax." **(Commissioner of Internal Revenue v. TMX Sales, Inc., et. al, supra.)**

Hence, since the claim for refund covers overpaid income tax for the fiscal year ending October 31, 1989, petitioner has two-years counted from February 15, 1990 (the date when the Final Income Tax Return was filed) to file a claim for refund. It has up to February 15, 1992 to file a claim for refund with the respondent and with this Court. Since the claim for refund was filed with respondent on February 21, 1991 and the petition for review was filed on April 3, 1991, it is therefore clear that the petition was filed on time.

With regard to the disallowance of accelerated depreciation in the amount of P 6,176,375.00, petitioner maintains that as a registered preferred pioneer enterprise it can avail of the incentives provided under Section 7(b) of R.A. No. 5186, to wit:

> "**Sec. 7. Incentives to a Registered Enterprise.** - A registered enterprise, to the extent engaged in a preferred area of investment, shall be granted the following incentive benefits.
>
> (a) xxx xxx xxx.
>
> (b) **Accelerated Depreciation.** - At the option of the taxpayer and in accordance with the procedure established by the Bureau of Internal Revenue, fixed assets may be (1) depreciated to the extent of not

> more than twice as fast as normal rate of depreciation or depreciated at normal rate of depreciation if expected life is ten years or less; or (2) depreciated over any number of years between five years and expected life if the latter is more than ten (10) years; and the depreciation thereon allowed as a deduction from taxable income: *Provided* that the taxpayer notifies the Bureau of Internal Revenue at the beginning of the depreciation period which depreciation rate allowed by this section will be used by it." [Underlining supplied.]

Being a preferred pioneer enterprise registered with the Board of Investments, petitioner availed the incentives provided under R.A. 5186 one of which is the use of the accelerated depreciation. In the course of the cross examination of respondent's witness, it was established that petitioner notified the BIR of its availment of the accelerated depreciation. No response was received thereafter from the Bureau. The records will also show that petitioner filed with the Bureau BIR Form No. 1702-E, indicating the nature of incentives availed of, that is, the accelerated depreciation.

R.A. 5186 prescribes a minimum requirement of notification and not approval by the BIR of the availment of the incentive adopting the accelerated depreciation. The option to use the accelerated depreciation is on the preferred pioneer enterprise. Having exercised its power of choice, petitioner's only obligation is to notify respondent of that choice. The law is clear on this regard. Petitioner can validly deduct the accelerated depreciation from its income. The same should not be disallowed.

Another item disallowed by the examiner refers to the repairs and maintenance in the total amount of P2,413,193.17. Because of the material amount involve, respondent's examiner contends that the same should be capitalized.

The repairs and maintenance cost must be ordinary and necessary business expense in order to be deductible from income. "The cost of incidental repairs, which neither materially add to the value of the property nor appreciably prolong its life and which were made to keep the property in an ordinarily efficient operating condition, may be deducted as an expense." (4 Mertens 372.) Other factors like the purpose for which the expenditures were made is also necessary in determining whether an item of expenditure should be capitalized or not. "If its purpose is merely to keep the property or a machine in efficient operating condition and is accordingly in the nature of a maintenance charge, it is ordinarily deductible. If it goes beyond that category, it is ordinarily non-deductible." (ibid., p.374) The amount should not be the controlling factor. Substance, not form, should be the controlling factor.

In this case, the Notes to Financial Statements of petitioner's audited financial report for the fiscal year 1989 indicates that the cost of maintenance and repairs is charged to income as incurred and significant renewals and betterment's are capitalized. (#1, Notes to Financial Statements, p. 47, CTA record.) Most of the items disallowed refer to spare parts, pinion gears, roller bearing, transformers and landed cost can be considered cost of machinery repairs. Spare parts are deemed to be replacement of worn-out parts the same is true with the rest of the items disallowed.

The amount of expenditure standing alone is not a sufficient base for determining whether an amount expended for repairs should be capitalized. "The presumption of correctness of assessment being a mere presumption cannot be made to rest on another presumption." **(Commissioner of Internal Revenue v. Benipayo, G.R. No. L-13656, Jan. 31, 1962; Island Garment Mfg. Corp. v. Commr. of Internal Revenue, CTA No. 2070, June 22, 1977; Medina v. CIR, CTA Case No. 1245, Dec. 27, 1971; Herrera v. Commr. of Internal Revenue, CTA Case No. 2060, June 27, 1972; Samson v. Commr. of Internal Revenue, CTA Case No. 232, June 30, 1958; Unterbo v. Commr. of Internal Revenue, CTA Case No. 363, Dec. 26, 1950.)** The disallowance of the aforesaid amount representing repairs and maintenance is erroneous.

WHEREFORE, finding the petition meritorious, respondent Commissioner of Internal Revenue is hereby ordered to **refund or** in the alternative, issue a **tax credit** certificate in favor of petitioner, Armco-Marsteel Alloy Corporation, in the amount of P5,061,899.00, representing overpaid income tax for the fiscal year ending October 31, 1989.

SO ORDERED.

Quezon City, Metro Manila, July 1, 1993.

Ernesto D. Acosta

ERNESTO D. ACOSTA
Presiding Judge

WE CONCUR:

MANUEL K. GRUBA
Associate Judge

RAMON O. DE VEYRA
Associate Judge

CERTIFICATION

I hereby certify that this decision was reached after due consultation among the members of the Court of Tax Appeals in accordance with Section 13, Article VIII of the Constitution.

ERNESTO D. ACOSTA
Presiding Judge