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REPUBLIC OF THE PHILIPPINES
Court of Tax Appeals
QUEZON CITY

EN BANC

COMMISSIONER OF INTERNAL REVENUE, Petitioner,	CTA E.B. NO. 648 (CTA CASE NO. 6819)
	Present:
- versus -	ACOSTA, *P.J.* CASTAÑEDA, JR., BAUTISTA, UY, CASANOVA, PALANCA-ENRIQUEZ, FABON-VICTORINO, MINDARO-GRULLA, *and* COTANGCO-MANALASTAS, *JJ.*
PHILIPPINE AIRLINES, INC. (PAL), Respondent.	
	Promulgated:
	DEC 15 2010 Apolinario 1:07 p.m.

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DECISION

UY, J.:

Before Us is a Petition for Review filed on June 29, 2010 seeking the reversal of the Decision dated January 5, 2010[1] and the Resolution dated June 3, 2010[2], respectively rendered by the First Division and the Special First Division of this Court (hereinafter collectively referred to as the "Court in Division") in CTA Case No. 6819, entitled *"Philippine Airlines, Inc. (PAL), petitioner, vs. Commissioner of Internal Revenue, respondent"*, the dispositive portions of which respectively read:

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[1] Penned by Associate Justice Caesar A. Casanova, and concurred by Presiding Justice Ernesto D. Acosta and Associate Justice Lovell R. Bautista. Docket, pp. 24 to 48.

[2] Docket, pp. 50 to 54.

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Decision dated January 5, 2010:

"**WHEREFORE,** premises considered, the instant **Petition for Review** and **Amended Petition for Review** are hereby **GRANTED**. Accordingly, the Formal Letter of Demand dated June 7, 2001 with Assessment Notice Nos. PT-98-000002, OTHT-98-000003, EWT-98-0000014, the Final Decision on Disputed Assessment for the payment of Deficiency Minimum Corporate Income Tax of PHP136,750,950.99, Deficiency Expanded Withholding Tax of PHP849,651,791.04 and VAT Compromise penalty of PHP100,000 or PHP25,000 per quarter are hereby **CANCELLED** and **WITHDRAWN**.

SO ORDERED."

Resolution dated June 3, 2010:

"**WHEREFORE**, finding no cogent reason to reverse the previous ruling of this Court, respondent's *Motion for Reconsideration* is hereby **DENIED** for lack of merit.

SO ORDERED."

THE FACTS

Petitioner is the government agency in charge of assessment and collection of all national internal revenue taxes, fees, and charges, including the 2% Minimum Corporate Income Tax on Domestic Corporation (MCIT), imposed under Section 27(E) of the National Internal Revenue Code (NIRC), and the Expanded Withholding Tax required under Section 57 also of the NIRC, with principal office at Bureau of Internal Revenue (BIR), National Office Building, Agham Road, Diliman, Quezon City.

On the other hand, respondent is a domestic corporation organized in accordance with the laws of the Republic of the Philippines with principal office at the 9th Floor, PAL Center, Legazpi Street, Legazpi Village, Makati City.

On July 15, 1998, respondent filed its Tentative Annual Income Tax Return for the fiscal year ended March 31, 1998, showing loss of

₱ 3,753,048,090.00 and unapplied excess creditable withholding tax of ₱ 1,028,248.00.

On May 20, 1999, respondent filed its Amended and Final Income Tax Return for the fiscal year ended March 31, 1998, showing a loss of ₱ 7,555,393,804.00, and unapplied excess creditable withholding tax of ₱ 1,028,248.00.

Respondent filed on July 26, 1999 with the office of petitioner a claim for refund dated July 15, 1999, of the unapplied expanded creditable withholding tax of ₱ 1,028,248.00 plus an additional amount of ₱ 33,018.00, or a total claim of ₱ 1,061,266.00.

Not receiving any response from petitioner, respondent filed on July 7, 2000 a Petition for Review with the Court in Division docketed as CTA Case No. 6134, praying that petitioner be ordered to refund respondent the above-mentioned amount of ₱ 1,061,266.00.

While the said petition for review was pending before the Court in Division, petitioner issued through the Large Taxpayers Service, Letter of Authority No. 00002139, dated August 10, 2000, authorizing the revenue officers named therein to investigate respondent's internal revenue tax liabilities for the fiscal year ending March 31, 1998.

On May 16, 2001, respondent received a Preliminary Assessment Notice issued by the Large Taxpayers Service, dated March 27, 2001, assessing respondent the amount of ₱ 1,624,206,679.32 as deficiency Franchise Tax, ₱ 678,905,498.33 as deficiency Expanded Withholding Tax, and ₱ 100,000.00 or

₱ 25,000.00 penalty for non-filing of quarterly summary list of sales and purchases.

On June 4, 2001, respondent, through its VP-Financial Services Department Marianne C. Raymundo, filed a written protest dated May 30, 2001, against the aforementioned proposed assessment, stating the reasons why respondent is not agreeable to the same.

On July 2, 2001, respondent received a Formal Letter of Demand dated June 7, 2001 from petitioner, with Assessment Notice Nos. PT-98-000002, OTHT-98-000003 and EWT-98-000014 demanding the payment of the total amount of ₱ 2,380,895,737.43, the details of which as shown in the said letter are quoted hereunder as follows:

"Assessment No. PT 98-000002

"A. Franchise Tax

	1997
Gross Taxable Income per books	PHP 52,389,133,788.68
Multiply by rate of tax	2%
Franchise Tax Due	1,047,782,675.77
Less: Tax Payments/credits	-
Basic tax still due	1,047,782,675.77
Add: 20% Interest per annum	628,669,605.46
Deficiency Franchise Tax	**1,676,452,281.23**

"Details of discrepancies:

Verification disclosed that gross taxable income per books amounted to P52,389,133,788.68. When multiplied by the rate of Franchise Tax of 2%, it resulted to a basic deficiency tax of P1,676.452.281.23. On the other hand, for income tax purposes, analysis of accounts per books disclosed that there is a deficiency basic income tax of P4,041,252,950,48. In accordance with Presidential Decree No. 1590, you are liable to income tax or franchise tax whichever is lower. You are therefore assessed the deficiency franchise tax.

"Assessment No. EWT 98-000014

"B. Expanded Withholding Tax

	1998
Basic Expanded withholding tax due	PHP 437,964,840.74
Add: 20% interest per annum	266,378,615.48
Deficiency Expanded Withholding Tax	**704,343,456.20**

"The withholding and remittance of creditable taxes withheld from various payors were properly complied with except for some income payments, which were not subjected to withholding tax. This resulted to a deficiency in the remittance of EWT in the amount of P704,343,456.20 inclusive of interest pursuant to Sec. 50 of the 1997 NIRC and its implementing regulations RR 2-98.

"C. Others

Upon audit, it was found out that no quarterly summary lists of sales and purchases were filed in violation of Sec. 3 of Revenue Regulations No. 6-89. Hence, you were assessed the amount of P100,000 or P25,000.00 for every violation in accordance with Revenue Memorandum Order No. 1-90."

On July 13, 2001, respondent wrote petitioner protesting the ₱ 2,380,896,737.43 assessment contained in its June 7, 2001 letter of demand.

Respondent received an undated letter from the OIC, Large Taxpayers Service of the BIR Estelita C. Aguirre, entitled "Final Decision on Disputed Assessment" on October 23, 2003 making reference to respondent's above-mentioned July 13, 2001 written protest and demanding the immediate payment of the amount of an adjusted deficiency tax assessment in the total amount of ₱ 986,502,742.03, which according to the said letter "is premised on the following":

"I. Deficiency Income Tax – MCIT P136,750,950.99

It was found out during the re-investigation that PAL incurred a total net loss of P6,410,894,815.79, therefore a deficiency MCIT on gross income was assessed pursuant to RR 9-98.

II. Deficiency Expanded Withholding Tax

Basic Expanded Withholding Tax Due	P 437,964,840.74
Interest from April 25, 1998 to July 15, 2001	266,378,615.46
Total Deficiency Expanded Withholding Per FAN	704,343,456.20
Add: Interest up to September 30, 2003	145,308,334.84
Total	849,651,791.05

Verification disclosed that there are certain income payments that were not subjected to expanded withholding tax in violation of Sec. 57 of NIRC and the implementing regulations of RR 2-98. Per re-investigation no adjustment was made in the original assessment, except for the adjustment in the computation of interest.

III. VAT-Compromise Penalty P100,000 or P25,000 per quarter for failure to file summary list sales and purchases in violation of Sec. 3 Revenue Regulation 6-98.

The records of this case disclosed that you have not introduced any documentary evidence to dispute the validity of our said findings."

Hence, respondent filed a Petition for Review with the Court in Division on November 21, 2003 docketed as CTA Case No. 6819[3] as the petitioner in said case. An Answer thereto was filed by the Commissioner of Internal Revenue on January 28, 2004 interposing several special and affirmative defenses.

After pre-trial held on April 30, 2004, the parties therein, through their counsels, submitted their Joint Stipulation of Facts and Issues on May 18, 2004 which was approved by the Court in Division in a Resolution dated June 9, 2004.

Philippine Airlines, Inc. then filed on January 31, 2005 a Motion for Summary Judgment praying that the assessment of its deficiency expanded withholding assessment of ₱ 849,651,791.04 and deficiency minimum corporate income tax assessment of ₱ 136,750,950.99 for the fiscal year ended March 31, 1998 be cancelled on the ground of prescription under Section 203 of the NIRC of 1997. The Commissioner of Internal Revenue filed its "Opposition (Re: Motion

[3] Philippine Airlines, Inc. (PAL), petitioner v. Commissioner of Internal Revenue, respondent.

for Summary Judgment)" on March 11, 2005, while a "Reply to Opposition to [Respondent's] Motion for Summary Judgment" was filed on April 7, 2005 by Philippine Airlines, Inc.

The said Motion was denied in the Resolution dated May 11, 2005 and the case was set for hearing for the initial presentation of respondent's evidence.

On October 28, 2005, Philippine Airlines, Inc. filed its Amended Petition for Review, while the Commissioner filed a Motion to Admit Amended Answer attaching thereto the Amended Answer on November 24, 2005. The same was admitted in the Resolution dated February 3, 2006. Philippine Airlines then filed on February 23, 2004 its Reply to the Amended Answer.

After the filing of the parties' respective Amended Pre-trial Briefs, an Amended Joint Stipulation of Facts and Issues was filed by the parties on August 25, 2006 wherein the genuineness, due execution and veracity of the following documents were admitted:

a. Letter of Authority No. 00002139 dated August 10, 2000;

b. Preliminary Assessment Notice dated March 27,2001;

c. Formal Letter of Demand dated June 7, 2001 together with the Final Assessment Notice;

d. Audit Result/Assessment Notice No. PT-98-000002 dated June 6, 2001;

e. Audit Result/Assessment Notice No. PT-98-00003 dated June 6, 2001;

f. Audit Result/Assessment Notice No. PT-98-00014 dated June 6, 2001; and

g. Final Decision on Disputed Assessment issued by the OIC-Large Taxpayers Service, Estelita C. Aguirre.

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The Court in Division approved the Amended Joint Stipulation of Facts and Issues in the Resolution dated August 28, 2006. After trial on the merits, the case was submitted for decision taking into consideration petitioner's "Memorandum" filed on August 7, 2009 and respondent's "Memorandum" filed on September 8, 2009.

On January 5, 2010, the assailed Decision was rendered by the Court in Division granting the Amended Petition for Review in CTA Case No. 6819 and cancelled and withdrew the Formal Letter of Demand dated June 7, 2001 with Assessment Notice Nos. PT-98-000002, OTHT-98-000003, EWT-98-0000014, the Final Decision on Disputed Assessment for the payment of Deficiency Minimum Corporate Income Tax of PHP136,750,950.99, Deficiency Expanded Withholding Tax of PHP849,651,791.04 and VAT Compromise penalty of PHP100,000 or PHP25,000 per quarter.

On January 29, 2010, the Commissioner filed a Motion for Reconsideration of said Decision, arguing, in essence, that the Court in Division erred in rendering the same, and thus, petitioner prayed for the reversal and setting aside thereof.

After the filing of the "Comment on [Petitioner's] Motion for Reconsideration" by Philippine Airlines, Inc. on February 12, 2010, the Court in Division denied the aforesaid motion in the assailed Resolution dated June 3, 2010.

Hence, this recourse before the Court *En Banc* by way of a Petition for Review, praying that the assailed Decision promulgated on January 5, 2010 and Resolution promulgated on June 3, 2010 be reversed and set aside, and another one be rendered ordering respondent to pay the amount of ₱ 986,502,742.03 representing deficiency 2% MCIT, deficiency expanded withholding tax, and VAT compromise penalty for fiscal year ending March 31, 1998, plus 25% surcharge for late payment and additional 20% interest from October 23, 2003 until fully paid pursuant to Sections 248 and 249 of the NIRC.

In the Resolution dated July 7, 2010,[4] the Court *En Banc* directed herein respondent to file a Comment thereto within ten (10) days from notice. On July 22, 2010, respondent filed its "Comment on Petitioner's Petition for Review"[5]. On July 29, 2010, the Court *En Banc* deemed the instant case submitted for decision.

Hence, this Decision.

THE ISSUE

The issue presented for the resolution of the Court *En Banc* is as follows:

> "WHETHER OR NOT THE FORMER FIRST DIVISION ERRED WHEN IT CANCELLED ASSESSMENT NOTICE NOS. PT-98-000002, OTHT-98-000003 AND EWT-98-000014 ASSESSING RESPONDENT FOR DEFICIENCY MINIMUM CORPORATE INCOME TAX (MCIT), EXPANDED WITHHOLDING TAX (EWT) AND VALUE-ADDED TAX (VAT) COMPROMISE PENALTY, RESPECTIVELY, IN THE TOTAL AMOUNT OF P986,502,742.03 FOR THE FISCAL YEAR ENDING 31 MARCH 1998."

Petitioner's Arguments

Petitioner argues that respondent is covered by Section 27(E) of the NIRC of 1997. Thus, respondent is liable for the computed deficiency MCIT of

[4] Docket, p. 59.
[5] Docket, pp. 61 to 82.

₱ 136,750,950.99 for fiscal year ending March 31, 1998.

According to petitioner, Revenue Memorandum Circular No. (RMC) 66-2003 did not alter, modify or amend the intent of the law insofar as the imposition of MCIT is concerned. The same circular merely clarifies the taxability of the respondent for income tax purposes as well as other franchise grantees similarly situated as existing law provides.

Petitioner further contends that the assessment for deficiency expanded withholding tax was issued within the prescriptive period. Allegedly, Section 58(C) of the NIRC of 1997 states categorically that the annual information return for creditable withholding taxes shall be filed not later than March 1 of the year following the year for which the annual return is being submitted. Since in this case the year for which respondent is being assessed for deficiency withholding taxes is 1998, respondent's annual information return is due on March 1, 1999. Thus, under Section 203 of the NIRC, petitioner has until March 1, 2002 within which to assess petitioner for expanded withholding tax.

Lastly, petitioner asserts that the assessment for compromise penalty of ₱ 100,000.00 or ₱ 25,000.00 per quarter is still reiterated for failure of respondent to file summary list of sales and purchases in violation of Section 3 of Revenue Regulations No. 6-98.

Respondent's Counter-Arguments

On the other hand, respondent counter-argues that the MCIT is imposed only on domestic and resident foreign corporations liable to the tax under the regular income tax system. Since respondent is not covered by such regular income tax system, it is likewise not covered by the provisions on MCIT under Section 27(E) of the NIRC of 1997.

Respondent also stresses that since the said Section 27(E) is not applicable to respondent despite the introduction thereof by Republic Act No. 8424 when the latter amended the NIRC, the more reason can it not be made to apply to respondent by the so-called "clarificatory" RMC 66-2003, because of the specific provision of Section 24 of respondent's franchise.

Respondent likewise points out that, in previous cases decided by this Court, We have already rejected petitioner's contention that the last day for filing the Annual Return by the withholding agent as required by Section 51(d) *[now Section 58(c)]* of the NIRC, is the date from which the three (3) year prescriptive period for issuing a deficiency withholding tax assessment should be counted.

Finally, according to respondent, it cannot be made to pay the ₱ 100,000 compromise penalty, since there was no conviction of respondent for violation of Section 254 of the NIRC, and that respondent did not voluntarily enter into a compromise with petitioner.

THE COURT EN BANC'S RULING

Respondent's exemption from the minimum corporate income tax (MCIT) is already a settled matter.

Section 27 of the NIRC of 1997 provides as follows:

"SEC. 27. *Rates of Income Tax on Domestic Corporations.*—

(A) *In General.*— Except as otherwise provided in this Code, an income tax of thirty-five percent (35%) is hereby imposed upon the **taxable income derived during each taxable year from all sources within and without the Philippines by every corporation**, as defined in

Section 22(B) of this Code and taxable under this Title as a corporation, organized in, or existing under the law of the Philippines: *Provided*, That effective January 1, 1998, the rate of income tax shall be thirty-four percent (34%); effective January 1, 1999, the rate shall be thirty-three percent (33%); **and effective January 1, 2000 and thereafter, the rate shall be thirty-two percent (32%)**.

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(E) *Minimum Corporate Income Tax on Domestic Corporations.*—

(1) *Imposition of Tax.*— **A minimum corporate income tax of two percent (2%) of the gross income as of the end of the taxable year**, as defined herein, is hereby imposed on a corporation taxable under this Title, beginning on the fourth taxable year immediately following the year in which such corporation commenced its business operations, when the minimum income tax is greater than the tax computed under Subsection (A) of this Section for the taxable year.

xxx xxx xxx." *(Emphases supplied)*

Based on the foregoing, a domestic corporation must pay whichever is the higher of: (1) the income tax under Section 27(A) of the NIRC of 1997, computed by applying the tax rate therein to the taxable income of the corporation; or (2) the MCIT under Section 27(E), also of the NIRC of 1997, equivalent to 2% of the gross income of the corporation. Although this may be the general rule in determining the income tax due from a domestic corporation under the NIRC of 1997, it can only be applied to respondent to the extent allowed by the provisions of its franchise.

Presidential Decree No. (PD) 1590, the franchise of respondent, contains provisions specifically governing its taxation, to wit:

"Section 13. In consideration of the franchise and rights hereby granted, the grantee shall pay to the Philippine Government during the life of this franchise **whichever of subsections (a) and (b) hereunder will result in a lower tax:**

(a) The **basic corporate income tax** based on the **grantee's annual net taxable income** computed in accordance with the provisions of the National Internal Revenue Code; or

(b) A **franchise tax of two per cent (2%) of the gross revenues derived by the grantee from all sources**, without distinction as to transport or nontransport operations; provided, that with respect to international air-transport service, only the gross passenger, mail, and freight revenues from its outgoing flights shall be subject to this tax.

The tax paid by the grantee under either of the above alternatives shall be **in lieu of all other taxes**, duties, royalties, registration, license, and other fees and charges of any kind, nature, or description, imposed, levied, established, assessed, or collected by any municipal, city, provincial, or national authority or government agency, now or in the future, including but not limited to the following:

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The grantee, shall, however, **pay the tax on its real property** in conformity with existing law.

For purposes of computing the basic corporate income tax as provided herein, the grantee is authorized:

(a) To **depreciate its assets** to the extent of **not more than twice** as fast the normal rate of depreciation; and

(b) To **carry over** as a deduction from taxable income **any net loss incurred in any year** up to five years following the year of such loss.

Section 14. The grantee shall pay either the franchise tax or the basic corporate income tax on quarterly basis to the Commissioner of Internal Revenue. Within sixty (60) days after the end of each of the first three quarters of the taxable calendar or fiscal year, the quarterly franchise or income-tax return shall be filed and payment of either the franchise or income tax shall be made by the grantee.

A final or an adjustment return covering the operation of the grantee for the preceding calendar or fiscal year shall be filed on or before the fifteenth day of the fourth month following the close of the calendar or fiscal year. The amount of the final franchise or income tax to be paid by the grantee shall be the balance of the total franchise or income tax shown in the final or adjustment return after deducting therefrom the total quarterly franchise or income taxes already paid during the preceding first three quarters of the same taxable year.

> Any excess of the total quarterly payments over the actual annual franchise of income tax due as shown in the final or adjustment franchise or income-tax return shall either be refunded to the grantee or credited against the grantee's quarterly franchise or income-tax liability for the succeeding taxable year or years at the option of the grantee.
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> The term **"gross revenue"** is herein defined as the total gross income earned by the grantee; (a) transport, nontransport, and other services; (b) earnings realized from investments in money-market placements, bank deposits, investments in shares of stock and other securities, and other investments; (c) total gains net of total losses realized from the disposition of assets and foreign-exchange transactions; and (d) gross income from other sources." *(Emphases supplied)*

According to the aforequoted provisions, the taxation of respondent, during the lifetime of its franchise, shall be governed by two fundamental rules, particularly: (1) respondent shall pay the Government either the basic corporate income tax or franchise tax, whichever is lower; and (2) the tax paid by respondent, under either of these alternatives, shall be in lieu of all other taxes, duties, royalties, registration, license, and other fees and charges, except only real property tax.

The basic corporate income tax of respondent shall be based on its annual net taxable income, computed in accordance with the NIRC. PD 1590 also explicitly authorizes respondent, in the computation of its basic corporate income tax, to (1) depreciate its assets twice as fast the normal rate of depreciation;[6] and (2) carry over as a deduction from taxable income any net loss incurred in any year up to five years following the year of such loss.[7]

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[6] As a general rule, there shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear (including reasonable allowance obsolescence) of property used in the trade or business. [Section 34(F) of the NIRC of 1997]

[7] In general, losses shall be deducted from gross income in the same taxable year said losses were incurred. The recognized exception under Section 39(D) of the NIRC of 1997, allowing net capital loss carryover, may only be availed of by a taxpayer "other than a corporation".

The franchise tax, on the other hand, shall be two per cent (2%) of the gross revenues derived by respondent from all sources, whether transport or nontransport operations. However, with respect to international air-transport service, the franchise tax shall only be imposed on the gross passenger, mail, and freight revenues of respondent from its outgoing flights.

Considering the foregoing precepts, the Supreme Court, in *Commissioner of Internal Revenue vs. Philippine Airlines, Inc.*,[8] has ruled that respondent cannot be subjected to MCIT for the following reasons, to wit:

> "*First*, Section 13(a) of Presidential Decree No. 1590 refers to **'basic corporate income tax.'** In *Commissioner of Internal Revenue v. Philippine Airlines, Inc.*,[9] the Court already settled that the 'basic corporate income tax,' under Section 13(a) of Presidential Decree No. 1590, relates to the general rate of 35% (reduced to 32% by the year 2000) as stipulated in Section 27(A) of the NIRC of 1997.
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> Section 13(a) of Presidential Decree No. 1590 requires that the basic corporate income tax be computed in accordance with the NIRC. This means that PAL shall compute its basic corporate income tax using the rate and basis prescribed by the NIRC of 1997 for the said tax. There is nothing in Section 13(a) of Presidential Decree No. 1590 to support the contention of the CIR that PAL is subject to the entire Title II of the NIRC of 1997, entitled 'Tax on Income.'
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> *Second*, Section 13(a) of Presidential Decree No. 1590 further provides that the basic corporate income tax of PAL shall be based on its **annual net taxable income**. This is consistent with Section 27(A) of the NIRC of 1997, which provides that the rate of basic corporate income tax, which is 32% beginning 1 January 2000, shall be imposed on the **taxable income** of the domestic corporation.
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> Taxable income is defined under Section 31 of the NIRC of 1997 as the **pertinent items of gross income specified in the said Code, less the deductions and/or personal and additional exemptions, if any, authorized for such types of income by the same Code or other special laws.** The gross income, referred to in Section 31, is described in Section 32 of the NIRC of 1997 as income from whatever source, including compensation for services; the conduct of trade or business or

[8] G.R. No. 180066, July 7, 2009.
[9] G.R. No. 160528, October 9, 2006.

the exercise of profession; dealings in property; interests; rents; royalties; dividends; annuities; prizes and winnings; pensions; and a partner's distributive share in the net income of a general professional partnership.

Pursuant to the NIRC of 1997, the taxable income of a domestic corporation may be arrived at by subtracting from gross income deductions authorized, not just by the NIRC of 1997, but also by special laws. Presidential Decree No. 1590 may be considered as one of such special laws authorizing PAL, in computing its annual net taxable income, on which its basic corporate income tax shall be based, to deduct from its gross income the following: (1) depreciation of assets at twice the normal rate; and (2) net loss carry-over up to five years following the year of such loss.

In comparison, the 2% MCIT under Section 27(E) of the NIRC of 1997 shall be based on the **gross income** of the domestic corporation. The Court notes that gross income, as the basis for MCIT, is given a special definition under Section 27(E)(4) of the NIRC of 1997, different from the general one under Section 34 of the same Code.

According to the last paragraph of Section 27(E)(4) of the NIRC of 1997, gross income of a domestic corporation engaged in the sale of service means **gross receipts, less sales returns, allowances, discounts and cost of services**. 'Cost of services' refers to all **direct costs and expenses** necessarily incurred to provide the services required by the customers and clients including (a) salaries and employee benefits of personnel, consultants, and specialists directly rendering the service; and (b) cost of facilities directly utilized in providing the service, such as depreciation or rental of equipment used and cost of supplies. Noticeably, inclusions in and exclusions/deductions from gross income for MCIT purposes are limited to those directly arising from the conduct of the taxpayer's business. It is, thus, more limited than the gross income used in the computation of basic corporate income tax.

In light of the foregoing, there is an apparent distinction under the NIRC of 1997 between taxable income, which is the basis for basic corporate income tax under Section 27(A); and gross income, which is the basis for the MCIT under Section 27(E). The two terms have their respective technical meanings, and cannot be used interchangeably. The same reasons prevent this Court from declaring that the basic corporate income tax, for which PAL is liable under Section 13(a) of Presidential Decree No. 1590, also covers MCIT under Section 27(E) of the NIRC of 1997, since the basis for the first is the annual net taxable income, while the basis for the second is gross income.

Third, even if the basic corporate income tax and the MCIT are both income taxes under Section 27 of the NIRC of 1997, and one is paid in place of the other, the two are distinct and separate taxes.

The Court again cites *Commissioner of Internal Revenue v. Philippine Airlines, Inc.*,[10] wherein it held that income tax on the passive income of a domestic corporation, under Section 27(D) of the NIRC of 1997, is different from the basic corporate income tax on the taxable income of a domestic corporation, imposed by Section 27(A), also of the NIRC of 1997. Section 13 of Presidential Decree No. 1590 gives PAL the option to pay basic corporate income tax or franchise tax, whichever is lower; and the tax so paid shall be in lieu of all other taxes, except real property tax. The income tax on the passive income of PAL falls within the category of 'all other taxes' from which PAL is exempted, and which, if already collected, should be refunded to PAL.

The Court herein treats MCIT in much the same way. Although both are income taxes, the MCIT is different from the basic corporate income tax, not just in the rates, but also in the bases for their computation. Not being covered by Section 13(a) of Presidential Decree No. 1590, which makes PAL liable only for basic corporate income tax, then MCIT is included in 'all other taxes' from which PAL is exempted.

That, under general circumstances, the MCIT is paid in place of the basic corporate income tax, when the former is higher than the latter, does not mean that these two income taxes are one and the same. The said taxes are merely paid in the alternative, giving the Government the opportunity to collect the higher amount between the two. The situation is not much different from Section 13 of Presidential Decree No. 1590, which reversely allows PAL to pay, whichever is lower of the basic corporate income tax or the franchise tax. It does not make the basic corporate income tax indistinguishable from the franchise tax.

Given the fundamental differences between the basic corporate income tax and the MCIT, presented in the preceding discussion, it is not baseless for this Court to rule that, pursuant to the franchise of PAL, said corporation is subject to the first tax, yet exempted from the second.

Fourth, the evident intent of Section 13 of Presidential Decree No. 1520 is to extend to PAL tax concessions not ordinarily available to other domestic corporations. Section 13 of Presidential Decree No. 1520 permits PAL to pay **whichever is lower** of the basic corporate income tax or the franchise tax; and the tax so paid shall be **in lieu of all other taxes**, except only real property tax. Hence, under its franchise, PAL is to pay the least amount of tax possible.

Section 13 of Presidential Decree No. 1520 is not unusual. A public utility is granted special tax treatment (including tax exceptions/exemptions) under its franchise, as an inducement for the

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[10] Supra.

acceptance of the franchise and the rendition of public service by the said public utility. In this case, in addition to being a public utility providing air-transport service, PAL is also the official flag carrier of the country.

The imposition of MCIT on PAL, as the CIR insists, would result in a situation that contravenes the objective of Section 13 of Presidential Decree No. 1590. In effect, PAL would not just have two, but three tax alternatives, namely, the basic corporate income tax, MCIT, or franchise tax. More troublesome is the fact that, as between the basic corporate income tax and the MCIT, PAL shall be made to pay **whichever is higher**, irrefragably, in violation of the avowed intention of Section 13 of Presidential Decree No. 1590 to make PAL pay for the lower amount of tax.

Fifth, the CIR posits that PAL may not invoke in the instant case the 'in lieu of all other taxes' clause in Section 13 of Presidential Decree No. 1520, if it did not pay anything at all as basic corporate income tax or franchise tax. As a result, PAL should be made liable for 'other taxes' such as MCIT. This line of reasoning has been dubbed as the Substitution Theory, and this is not the first time the CIR raised the same. The Court already rejected the Substitution Theory in *Commissioner of Internal Revenue v. Philippine Airlines, Inc.*,[11] to wit:

> ***'Substitution Theory' of the CIR Untenable***
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> **A careful reading of Section 13 rebuts the argument of the CIR that the 'in lieu of all other taxes' proviso is a mere incentive that applies only when PAL actually pays something.** It is clear that PD 1590 intended to give respondent the option to avail itself of Subsection (a) or (b) as consideration for its franchise. Either option excludes the payment of other taxes and dues imposed or collected by the national or the local government. PAL has the option to choose the alternative that results in lower taxes. **It is not the fact of tax payment that exempts it, but the exercise of its option.**
>
> Under Subsection (a), the basis for the tax rate is respondent's annual net taxable income, which (as earlier discussed) is computed by subtracting allowable deductions and exemptions from gross income. By basing the tax rate on the annual net taxable income, PD 1590 necessarily recognized the situation in which taxable income may result in a negative amount and thus translate into a zero tax liability.

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[11] Supra.

> Notably, PAL was owned and operated by the government at the time the franchise was last amended. It can reasonably be contemplated that PD 1590 sought to assist the finances of the government corporation in the form of lower taxes. When respondent operates at a loss (as in the instant case), no taxes are due; in this instances, it has a lower tax liability than that provided by Subsection (b).
>
> **The fallacy of the CIR's argument is evident from the fact that the payment of a measly sum of one peso would suffice to exempt PAL from other taxes, whereas a zero liability arising from its losses would not. There is no substantial distinction between a zero tax and a one-peso tax liability.** (Emphasis ours.)

Based on the same ratiocination, the Court finds the Substitution Theory unacceptable in the present Petition.

The CIR alludes as well to Republic Act No. 9337, for reasons similar to those behind the Substitution Theory. Section 22 of Republic Act No. 9337, more popularly known as the Expanded Value Added Tax (E-VAT) Law, abolished the franchise tax imposed by the charters of particularly identified public utilities, including Presidential Decree No. 1590 of PAL. PAL may no longer exercise its options or alternatives under Section 13 of Presidential Decree No. 1590, and is now liable for both corporate income tax and the 12% VAT on its sale of services. The CIR alleges that Republic Act No. 9337 reveals the intention of the Legislature to make PAL share the tax burden of other domestic corporations.

The CIR seems to lose sight of the fact that the Petition at bar involves the liability of PAL for MCIT for the fiscal year ending **31 March 2001**. Republic Act No. 9337, which took effect on **1 July 2005**, cannot be applied retroactively and any amendment introduced by said statute affecting the taxation of PAL is immaterial in the present case.

And sixth, Presidential Decree No. 1590 explicitly allows PAL, in computing its basic corporate income tax, to carry over as deduction any net loss incurred in any year, up to five years following the year of such loss. Therefore, Presidential Decree No. 1590 does not only consider the possibility that, at the end of a taxable period, PAL shall end up with **zero annual net taxable income** (when its deductions exactly equal its gross income), as what happened in the case at bar, but also the likelihood that PAL shall incur **net loss** (when its deductions exceed its gross income). If PAL is subjected to MCIT, the provision in Presidential Decree No. 1590 on net loss carry-over will be rendered nugatory. Net loss carry-over is material only in computing the annual net taxable income to be used as basis for the basic corporate income tax of PAL; but PAL will never be able to avail itself of the basic corporate income tax option when it is in a net loss position, because it will always then be compelled to pay the necessarily higher MCIT.

Consequently, the insistence of the CIR to subject PAL to MCIT cannot be done without contravening Presidential Decree No. 1520.

Between Presidential Decree No. 1520, on one hand, which is a special law specifically governing the franchise of PAL, issued on 11 June 1978; and the NIRC of 1997, on the other, which is a general law on national internal revenue taxes, that took effect on 1 January 1998, the former prevails. The rule is that on a specific matter, the special law shall prevail over the general law, which shall be resorted to only to supply deficiencies in the former. In addition, where there are two statutes, the earlier special and the later general – the terms of the general broad enough to include the matter provided for in the special – the fact that one is special and the other is general creates a presumption that the special is to be considered as remaining an exception to the general, one as a general law of the land, the other as the law of a particular case. It is a canon of statutory construction that a later statute, general in its terms and not expressly repealing a prior special statute, will ordinarily not affect the special provisions of such earlier statute.

xxx xxx xxx

The MCIT was a new tax introduced by Republic Act No. 8424. Under the doctrine of strict interpretation, the burden is upon the CIR to primarily prove that the new MCIT provisions of the NIRC of 1997, clearly, expressly, and unambiguously extend and apply to PAL, despite the latter's existing tax exemption. To do this, the CIR must convince the Court that the MCIT is a basic corporate income tax, and is not covered by the 'in lieu of all other taxes' clause of Presidential Decree No. 1590. Since the CIR failed in this regard, the Court is left with no choice but to consider the MCIT as one of 'all other taxes,' from which PAL is exempt under the explicit provisions of its charter."

Based on the foregoing, We are convinced that respondent is exempt from the MCIT imposed under Section 27(E) of the NIRC of 1997. Thus, respondent cannot be held liable for the assessed deficiency MCIT of ₱ 136,750,950.99 for fiscal year ending March 31, 1998.

RMC 66-2003 is not binding on this Court.

In support of the argument that respondent is liable for the MCIT, petitioner attempts to convince this Court to adhere to RMC 66-2003, since "[w]hen an administrative agency renders an opinion by means of a circular or memorandum, it merely interprets a pre-existing law, and no publication is necessary for its validity. Construction by an executive branch of government of a particular law although not binding upon the courts must be given weight as the construction comes from the branch of the government called upon to implement the law."[12]

We are not persuaded.

It is significant to note that RMC 66-2003 was issued only on October 14, 2003, more than five (5) years after fiscal year 1997-1998 of respondent ended on March 31, 1998. This violates the well-entrenched principle that statutes, including administrative rules and regulations, operate prospectively only, unless the legislative intent to the contrary is manifest by express terms or by necessary implication.[13]

Furthermore, in the same above-quoted case of *Commissioner of Internal Revenue vs. Philippine Airlines, Inc.*, the High Court likewise ruled on the value of RMC 66-2003, to wit:

> "xxx despite the claims of the CIR that RMC No. 66-2003 is just a clarificatory and internal issuance, the Court observes that RMC No. 66-2003 does more than just clarify a previous regulation and goes beyond mere internal administration. It effectively increases the tax burden of PAL and other taxpayers who are similarly situated, making them liable for a tax for which they were not liable before. Therefore, RMC No. 66-2003 cannot be given effect without previous notice or publication to those who will be affected thereby. In *Commissioner of Internal Revenue v. Court of Appeals*,[14] the Court ratiocinated that:

[12] Petition for Review, Docket, p. 15.
[13] *BPI Leasing Corporation vs. Court of Appeals*, 461 Phil. 451, 460 (2003).
[14] 329 Phil. 987, 1007-1009 (1996)

It should be understandable that when an administrative rule is merely interpretative in nature, its applicability needs nothing further than its bare issuance for it gives no real consequence more than what the law itself has already prescribed. **When, upon the other hand, the administrative rule goes beyond merely providing for the means that can facilitate or render least cumbersome the implementation of the law but substantially adds to or increases the burden of those governed, it behooves the agency to accord at least to those directly affected a chance to be heard, and thereafter to be duly informed, before that new issuance is given the force and effect of law.**

A reading of RMC 37-93, particularly considering the circumstances under which it has been issued, convinces us that the circular cannot be viewed simply as a corrective measure (revoking in the process the previous holdings of past Commissioners) or merely as construing Section 142(c)(1) of the NIRC, as amended, but has, in fact and most importantly, been made in order to place 'Hope Luxury,' 'Premium More' and 'Champion' within the classification of locally manufactured cigarettes bearing foreign brands and to thereby have them covered by RA 7654. Specifically, the new law would have its amendatory provisions applied to locally manufactured cigarettes which at the time of its effectivity were not so classified as bearing foreign brands. Prior to the issuance of the questioned circular, 'Hope Luxury,' 'Premium More,' and 'Champion' cigarettes were in the category of locally manufactured cigarettes not bearing foreign brand subject to 45% ad valorem tax. Hence, without RMC 37-93, the enactment of RA 7654, would have had no new tax rate consequence on private respondent's products. Evidently, in order to place 'Hope Luxury,' 'Premium More,' and 'Champion' cigarettes within the scope of the amendatory law and subject them to an increased tax rate, the now disputed RMC 37-93 had to be issued. **In so doing, the BIR not simply interpreted the law; verily, it legislated under its quasi-legislative authority. The due observance of the requirements of notice, of hearing, and of publication should not have been then ignored.**

Indeed, the BIR itself, in its **RMC 10-86**, has observed and provided:

'RMC NO. 10-86

Effectivity of Internal Revenue Rules and Regulations "It has been observed that one of the problem areas bearing on compliance with Internal

> Revenue Tax rules and regulations is lack or insufficiency of due notice to the tax paying public. **Unless there is due notice, due compliance therewith may not be reasonably expected.** And most importantly, their strict enforcement could possibly suffer from legal infirmity in the light of the constitutional provision on 'due process of law' and the essence of the Civil Code provision concerning effectivity of laws, whereby due notice is a basic requirement (Sec. 1, Art. IV, Constitution; Art. 2, New Civil Code).
>
> 'In order that there shall be a just enforcement of rules and regulations, **in conformity with the basic element of due process, the following procedures are hereby prescribed** for the drafting, issuance and implementation of the said Revenue Tax Issuances:
>
> '(1). This Circular shall apply only to (a) Revenue Regulations; (b) Revenue Audit Memorandum Orders; and (c) **Revenue Memorandum Circulars** and Revenue Memorandum Orders bearing on internal revenue tax rules and regulations.
>
> '(2). Except when the law otherwise expressly provides, the aforesaid internal revenue tax issuances **shall not begin to be operative until after due notice thereof may be fairly presumed**.
>
> 'Due notice of the said issuances may be fairly presumed only after the following procedures have been taken:
>
> 'xxx xxx xxx "(5). Strict compliance with the foregoing procedures is enjoined.
>
> Nothing on record could tell us that it was either impossible or impracticable for the BIR to observe and comply with the above requirements before giving effect to its questioned circular. (Emphases ours.)

The Court, however, stops short of ruling on the validity of RMC No. 66-2003, for it is not among the issues raised in the instant Petition. It only wishes to stress the requirement of prior notice to PAL before RMC No. 66-2003 could have become effective. Only after RMC No. 66-2003 was issued on 14 October 2003 could PAL have been given notice of said circular, and only following such notice to PAL would RMC No. 66-2003 have taken effect. Given this sequence, it is not possible to say that RMC No. 66-2003 was already in effect and should have been strictly complied with by PAL for its fiscal year which ended on 31 March 2001.

Even conceding that the construction of a statute by the CIR is to be given great weight, the courts, which include the CTA, are not bound thereby if such construction is erroneous or is clearly shown to be in conflict with the governing statute or the Constitution or other laws. 'It is the role of the Judiciary to refine and, when necessary, correct constitutional (and/or statutory) interpretation, in the context of the interactions of the three branches of the government.' xxx."

The assessment for deficiency expanded withholding tax was not issued within the prescriptive period.

Section 203 of the NIRC of 1997 provides as follows:

"SEC. 203. *Period of Limitation Upon Assessment.*— Except as provided in Section 222, **internal revenue taxes shall be assessed within three (3) years after the last day prescribed by law for the filing of the return**, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period: *Provided*, That in a case where a return is filed beyond the period prescribed by law, the three (3)-year period shall be counted from the day the return was filed. For purposes of this Section, a return filed before the last day prescribed by law for the filing thereof shall be considered as filed on such last day." *(Emphasis supplied)*

Based on the foregoing, it is clear that the BIR has three (3) years, counted from the date of actual filing of the return or from the last date prescribed by law for the filing of such return, whichever comes later, to assess a national internal revenue tax or to begin a court proceeding for the collection thereof without an assessment. Simply put, the counting of the three-year period depends on the filing of the pertinent return.

Parenthetically, the deficiency withholding tax assessment in question covers the period April 1997 to March 1998. Thus, considering that the NIRC of 1997 took effect only on January 1, 1998, the provisions thereof concerning the filing of the withholding tax returns shall be applied for the assessments covering the months of January to March of 1998; while on the remainder, the pertinent provisions of the NIRC of 1977, as amended should apply.

The following comparison, however, of the pertinent provisions of the NIRC of 1977, as amended, and the NIRC of 1997 reveals that both law required two (2) types of "returns" that need to be filed by a withholding agent: (1) a *quarterly return*, which is immediately filed after and near the date when the taxes are deducted and withheld, and (2) an *annual information return*, which is filed at the end of the year, to wit:

NIRC of 1977, as amended	NIRC of 1997
"SEC. 51. *Return and payment of taxes withheld at source.—* (a) *Quarterly returns and payment of taxes withheld.—* Taxes deducted and withheld under Section 50 shall be covered by a return and paid to the Revenue District Officer, Collection Agent, or duly authorized Treasurer of the city, or municipality where the withholding agent has his legal residence or principal place of business, or where the withholding agent is a corporation, where the principal office is located. xxx. The Commissioner of Internal Revenue may, with the approval of the Secretary of Finance, require these withholding agents to pay or deposit the taxes deducted and withheld at more frequent intervals when necessary to protect the interest of the Government. The return for final withholding tax shall be filed and the payment made within 25 days from the close of each calendar quarter, while the return for creditable withholding taxes shall be filed and the payment made not later than the last day of the month following	"SEC. 58. *Returns and Payment of Taxes Withheld at Source.—* (A) *Quarterly Returns and Payments of Taxes Withheld.—* Taxes deducted and withheld under Section 57 by withholding agents shall be covered by **a return** and paid to, except in cases where the Commissioner otherwise permits, an authorized agent bank, Revenue District Officer, Collection Agent, or duly authorized Treasurer of the city or municipality where the withholding agent has his legal residence or principal place of business, or where the withholding agent is a corporation, where the principal office is located. xxx xxx xxx The return for final withholding tax shall be filed and the payment made within twenty-five (25) days from the close of each calendar quarter, while **the return for creditable withholding taxes shall be filed and the payment made not later than the last day of the month following the close of the**

the close of the quarter during which the withholding was made. xxx xxx xxx (c) ***Annual returns***.— Every withholding agent required to deduct and withhold taxes under Section 50 shall submit to the Commissioner of Internal Revenue **a reconciliation statement of quarterly payments and list of payees and income payments**. In the case of final withholding taxes, the return shall be filed on or before January 31 of the succeeding year, and for creditable withholding taxes, not later than March 1 of the year following the year for which the **annual report** is being submitted. xxx." *(Emphases supplied)*	**quarter during which withholding was made:** ***Provided***, **That the Commissioner, with the approval of the Secretary of Finance, may require these withholding agents to pay or deposit the taxes deducted or withheld at more frequent intervals when necessary to protect the interest of the government.** xxx xxx xxx (C) *Annual Information Return.*— Every withholding agent required to deduct and withhold taxes under Section 57 shall submit to the Commissioner an **annual information return containing the list of payees and income payments, amount of taxes withheld from each payee and such other pertinent information as may be required by the Commissioner**. In the case of final withholding taxes, the return shall be filed on or before January 31 of the succeeding year, and **for creditable withholding taxes, not later than March 1 of the year following the year for which the annual report is being submitted.** xxx. xxx xxx xxx." *(Emphases supplied)*

It is noteworthy that instead of on a quarterly basis, the returns referred to in the aforequoted Section 51(a) of the NIRC of 1977, as amended, and Section 58(A) of the NIRC of 1997 were made to be filed on a *monthly* basis, pursuant to their respective implementing rules as follows:

Section 2 of Revenue Regulations No. (RR) 5-85, as amended by RR 3-93	Section 2.58(2)(a) of RR 2-98
"Taxes deducted and withheld on: xxx xxx xxx	"The withholding tax return, whether creditable or final, shall be filed and

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(j) income payments subject to the creditable (expanded) withholding taxes; and (k) income subject to final withholding taxes shall be remitted **within ten (10) days after the end of each calendar month** with the filing of appropriate return (BIR Form 1743-W). However, taxes withheld from the last compensation/**income payment for the calendar year (December) shall be remitted on or before the 25th day of January of the succeeding year**." *(Emphases supplied)*	payments should be made **within ten (10) days after the end of each month except for taxes withheld for December which shall be filed on or before January 25 of the following year**." *(Emphases supplied)*

Such being the case, there are two (2) types of "returns" that need to be filed by a withholding agent, under the old and new law, viz: (1) a *monthly return*, which is immediately filed after and near the date when the taxes are deducted and withheld, and (2) an *annual information return*, which is filed at the end of the year. As stated, the former is filed on or before the 10th day after the end of each month except taxes withheld for December which shall be filed on or before January 25 of the following year; while the latter is filed on or before March 1 of the year following the year for which the annual report is being submitted.

Since Section 203 of the NIRC of 1997 does not specify as to which of the said two (2) returns should be used in computing the three-year period, the pivotal question is: to which of the filing of the said two returns should the three-year period be reckoned?

As earlier observed, petitioner is of the view that the said three-year period should be reckoned from the filing of the *annual information return*. Respondent, however, takes the contrary view, and opines that the three-year period should be counted from the filing of the *monthly returns*.

Admittedly, the law is silent as to which of the said returns should be used. However, to guide Us in choosing one either of the two returns, We look unto the purpose of the statute of limitation under the said Section 203. Existing jurisprudence[15] establishes that it is to safeguard the interest of the taxpayer against unreasonable investigation. Unreasonable investigation contemplates cases where the period for assessment extends indefinitely because this deprives the taxpayer of the assurance that it will no longer be subjected to further investigation for taxes after the expiration of a reasonable period of time. Thus, the law on prescription, being a remedial measure, should be liberally construed in order to afford such protection.[16] In other words, to give effect to the legislative intent, the provisions on the statute of limitations on assessment and collection of taxes shall be construed and applied in favor of the taxpayer and strictly against the Government.[17]

Such being the case, since the said *monthly return* is filed earlier than the *annual information return*, and accordingly, earlier in time to be subject to the three-year prescriptive period under Section 203 of the NIRC of 1997, the counting of such three-year period should be reckoned from the filing of the same *monthly return* required under Section 58(A) of the NIRC of 1997 in relation to Section 2.58(2)(a) of RR 2-98, insofar as the assessment of withholding taxes are concerned.

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[15] *Philippine Journalist, Inc. vs. Commissioner of Internal Revenue*, G.R. No. 162852, December 16, 2004; *Bank of the Philippine Islands vs. Commissioner of Internal Revenue*, G.R. No. 139736, October 17, 2005; *Commissioner of Internal Revenue vs. Philippine Global Communications, Inc.*, G.R. No. 167146, October 31, 2006.
[16] *Commissioner of Internal Revenue vs. B.F. Goodrich Phils., Inc., et al.*, G.R. No. 164171, February 4, 1999; *Commissioner of Internal Revenue vs. Philippine Global Communications, Inc.*, supra.
[17] *Bank of the Philippine Islands vs. Commissioner of Internal Revenue*, supra.

Accordingly, the last day of the statute of limitation for each month covering the period from April 1997 to March 1998 are summarized as follows:

Period	Last Day to File Return	Date filed	Last Day to Assess
April 1997	May 10, 1997	May 27, 1997	May 27, 2000
May 1997	June 10, 1997	June 25, 1997	June 25, 2000
June 1997	July 10, 1997	July 25, 1997	July 25, 2000
July 1997	August 10, 1997	August 25, 1997	August 25, 2000
August 1997	September 10, 1997	September 25, 1997	September 25, 2000
September 1997	October 10, 1997	October 27, 1997	October 27, 2000
October 1997	November 10, 1997	November 25, 1997	November 25, 2000
November 1997	December 10, 1997	December 29, 1997	December 29, 2000
December 1997	January 25, 1998	January 26, 1998	January 26, 2001
January 1998	February 10, 1998	February 25, 1998	February 25, 2001
February 1998	March 10, 1998	March 25, 1998	March 25, 2001
March 1998	April 10, 1998	April 27, 1998	April 27, 2001

Considering that the Formal Letter of Demand dated June 7, 2001 with Notice of Assessment (No. EWT-98-000014) for the expanded withholding tax was received by respondent only on July 2, 2001,[18] the subject assessment for the period covering April 1997 to March 1998 was clearly made beyond the three (3)-year prescriptive period as mandated by law.

Compromise penalty should not be imposed.

Anent the imposition of compromise penalty of ₱ 100,000.00 or ₱ 25,000.00 per quarter, the same should be cancelled. This must be so because compromise penalties are only amounts suggested in settlement of criminal liability, and may not be imposed or exacted on the taxpayer in the event that a taxpayer refuses to pay the same.[19] In other words, compromise penalties imply mutual agreement between the taxpayer, on one hand, and the

[18] Exhibits "H", "H-3", and "H-4", Division Docket, pp. 27 to 28, 31.
[19] Revenue Memorandum Order No. 1-90.

Commissioner of Internal Revenue, on the other.[20] Thus, since in this case, there is no indication that petitioner is willing to pay the said amount, the same should not be imposed.

WHEREFORE, all the foregoing considered, the instant Petition for Review is hereby **DENIED** for lack of merit. The assailed Decision promulgated on January 5, 2010 and Resolution dated June 3, 2010 by the Court in Division, are hereby **AFFIRMED**.

SO ORDERED.

ERLINDA P. UY
Associate Justice

WE CONCUR:

ERNESTO D. ACOSTA
Presiding Justice

JUANITO C. CASTAÑEDA, JR.
Associate Justice

LOVELL R. BAUTISTA
Associate Justice

CAESAR A. CASANOVA
Associate Justice

OLGA PALANCA-ENRIQUEZ
Associate Justice

ESPERANZA R. FABON-VICTORINO
Associate Justice

Cielito N. Mindaro-Grulla
CIELITO N. MINDARO-GRULLA
Associate Justice

AMELIA R. COTANGCO-MANALASTAS
Associate Justice

[20] Refer to *Dr. Felisa L. Vda. De San Agustin, in substitution of Jose Y. Feria, in his capacity as Executor of the Estate of Jose San Agustin vs. Commissioner of Internal Revenue*, G.R. No. 138485, September 10, 2001.

CERTIFICATION

Pursuant to Section 13, Article VIII of the Constitution, it is hereby certified that the conclusions in the above decision were reached in consultation before the case was assigned to the writer of the opinion of the Court *En Banc*.

ERNESTO D. ACOSTA
Presiding Justice