REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

M.E. HOLDING CORPORATION,
Petitioner,

- versus -

C.T.A. CASE NO. 6052

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:
MAY 2 1 2002

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DECISION

This Petition for Review involves a claim for the refund of the amount of P684,151.00 allegedly representing overpaid corporate income tax for the taxable year 1997 arising from the erroneous treatment of the 20% sales discounts granted to senior citizens as deduction from gross income rather than as tax credit.

The facts of the case as culled from the records are as follows:

Petitioner M. E. Holding Corporation is a domestic corporation organized and existing under the laws of the Philippines with principal office address at No. 7 Mercury Avenue, Bagumbayan, Quezon City *(Item No. 1, Joint Stipulation of Facts, CTA records p. 41).*

In 1997, petitioner operated two (2) "Mercury Drug" franchise drug stores: one located at Session Road, Baguio City and the other at Magsaysay, Baguio City. It is duly licensed to operate the said drug stores by the Bureau of Food and Drugs, the local government units where the drugstores are located, the Department of Trade and Industry

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and the Bureau of Internal Revenue *(Items No. 2 & 3, Joint Stipulation of Facts, CTA records, p.41)*.

Petitioner alleged that pursuant to Republic Act No. 7432, otherwise known as the "Senior Citizens Act," it granted 20% sales discounts on medicines sold to qualified senior citizens during the calendar year 1997, totalling P1,052,539.00 *(par. 5, Petition for Review, CTA records, p.2)*. According to petitioner, in its 1997 annual income tax return filed on April 15, 1998, it was forced to claim the amount representing the 20% sales discounts as a deduction from its gross income pursuant to Section 2(i) of Revenue Regulations No. 2-94, which implements Section 4 of Republic Act (R.A.) No. 7432, instead of claiming the same as tax credit/refund.

However, it is petitioner's view that Section 2(i) of Revenue Regulations No. 2-94 erroneously implements Section 4(a) of R.A. No. 7432 which clearly provides that the cost of the 20% sales discounts to senior citizens may be claimed as tax credit and not as a deduction from gross income. Thus, on the same day that it filed its 1997 annual income tax return, petitioner filed a letter protesting the erroneous treatment of the 20% sales discounts to senior citizens as deduction from gross income rather than as tax credit *(Exhibit E)*.

On March 19, 1999, petitioner filed with the BIR a formal claim for tax refund or credit of its alleged overpaid income tax for taxable year 1997 in the amount of P684,151.00 computed as follows *(Exhibit F)*:

Net Sales		P 108,693,107.00
Add: 20% Sales Discount to Senior Citizens		1,052,539.00
Gross Sales		P 109,745,646.00
Less: Cost of Sales		
Merchandise inventory, beginning	P 11,937,299.00	

Purchases	100,486,273.00	
Total merchandise available for sale	P112,423,572.00	
Less: Merchandise inventory, end	13,555,792.00	98,867,780.00
Gross Profit		P 10,877,866.00
Add: Miscellaneous Income		97,549,522.00
Total Income		P 108,427,388.00
Less: Operating Expenses		21,091,724.00
Net Income before Income Tax		P 87,335,664.00
Less: Income subjected to Final Tax		72,396,417.00
Net Taxable Income		P 14,939,247.00
Income Tax Due		P 5,228,736.00
Less: Tax Credit – Cost of 20% Discount to Senior Citizens		1,052,539.00
Income Tax Refundable/Overpaid Income Tax		P 4,176,197.00
Less: Income Tax Actually Paid		4,860,348.00
Income Tax Refundable/Overpaid Income Tax		P 684,151.00

Failing to obtain an affirmative relief from the respondent, petitioner comes to this Court on April 6, 2000 and filed a petition for review in order to toll the running of the two-year prescriptive period within which to file a judicial action for tax credit/refund.

In his Answer filed on May 25, 2000, respondent specifically denied petitioner's material allegations and set up the following special and affirmative defenses, to wit:

> "4 In an action for refund, the taxpayer has the burden to show that the taxes paid were erroneously or illegally collected and failure to do so is fatal to the action;
>
> 5. Claims for tax refund are strictly construed against the taxpayer. Petitioner has no cause of action."

As stipulated by the parties, the issues to be resolved by this Court are as follows:

1. Whether the 20% sales discount granted to senior citizens on their purchase of medicines should be treated as a tax credit deductible from the tax due as provided under R.A. 7432 or merely as a deduction from gross income as provided under Revenue Regulations No. 2-94.

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2. Whether or not petitioner actually granted a total amount of SIX HUNDRED EIGHTY FOUR THOUSAND ONE HUNDRED FIFTY ONE PESOS (P 684,151.00) sales discounts to senior citizens on their purchases of medicines in the year 1997.

3. Whether or not petitioner is entitled to a tax credit/refund in the amount of SIX HUNDRED EIGHTY FOUR THOUSAND ONE HUNDRED FIFTY ONE PESOS (P 684,151.00).

The legal issue besetting the case at bar is not one of first impression. In fact, in previous cases of similar nature, this Court upheld the treatment of the 20% sales discounts to senior citizens as tax credit deductible from the tax due instead of mere deductions from gross income, thus:

> "A cursory review of the wordings of Section 4 of Republic Act No. 7432 would reveal that the law literally intended the cost of the 20% discount to be claimed as tax credit by private establishments. We could not see any plausible reason for the respondent to interpret the phrase in a different way. The discount being available for tax credit as stated in the law cannot be made incoherent to mean that such discount be utilized instead as a deduction from gross income and from gross sales as what is provided in Revenue Regulations No. 2-94.
>
> To be valid, an administrative regulation must not be in contravention but should conform to the standards that the law prescribes (*Tayug Rural Bank vs. Central Bank 146 SCRA 120*). Its promulgation must be authorized by the legislature (Philippine Administrative Law, Cruz , 1994 ed., p. 32).
>
> RR No. 2-94 which engraved a new meaning to the phrase "tax credit" as referring to the 20% discount which is deductible from gross sales is patently incongruous and a deviation from the plain intendment of the law. It is even repugnant to the common dictionary acceptation of said phrase.
>
> In declaring that the provisions of RA 7432 prevail over Revenue regulations No. 2-94, it is important to point out that the cost of the 20%

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discount shall not be treated as deduction from the gross income of the petitioner nor deducted from its gross sales for VAT or other percentage tax purposes. The benefit that can be derived by taxpayers is the privilege of claiming these discounts as tax credit and no longer as deductions as what other taxpayers have done. They cannot avail of tax credit and claim said discounts as deductions at the same time because this would be tantamount to granting them benefits that are already disproportionate to the obligations imposed upon them by virtue of said law. This is to make clear for both the taxpayers and respondent that the tax credit privilege takes the place of claiming these discounts as deductions pursuant to this Court's stand that Section 2(i) of Revenue Regulations 2-94 is null and void and it is Section 4(a) of RA 7432 that will apply in cases of this nature." (*Mercury Drug Corporation vs. Commissioner of Internal Revenue, CTA Case No. 5612, January 9, 2001; Mercury Drug Corporation vs. CIR, CTA Case No. 5315, September 6, 2000; Trinity Franchising and Management Corporation vs. Commissioner of Internal Revenue, CTA Case No. 5605, May 30, 2000; M.E. Holding Corporation vs. Commissioner of Internal Revenue, CTA Case No. 5604, April 25, 2000; Vas Salus Drug Corporation vs. Commissioner of Internal Revenue, CTA Case No. 5509, November 26, 1999; Trinity Franchising and Management Corporation vs. CIR, CTA Case No. 5313, promulgated August 18, 1998; M.E. Holding Corporation vs. CIR, CTA Case No. 5314, August 17, 1998; Baliuag Drug Corporation vs. CIR, CTA Case No. 5365, May 13, 1998; Del Rosario Drug Corporation vs CIR, CTA Case No. 5357, April 6, 1998; and Sto. Rosario Drug Corporation vs. CIR, CTA Case No. 5367, February 16, 1998*)

The Court of Appeals affirmed the preceding declaration in several cases appealed before it (*Commissioner of Internal Revenue vs. Elmas Drug Corporation, CA-G.R. SP No. 49946, October 19, 1999; Trinity Franchising and Management Corporation vs. Commissioner of Internal Revenue, CA-G.R. SP NO. 60269, April 4, 2001; The Commissioner of Internal Revenue vs. Bicolandia Drug Corporation, CA G.R. SP No. 62824, May 3, 2001 and Central Luzon Drug Corporation vs. Commissioner of Internal Revenue, CA-G.R. SP No. 60057, dated May 31, 2001)*, the latest of which is the case of **Commissioner of Internal Revenue vs. Bicolandia Drug Company (formerly known**

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as Elmas Drug Corporation), CA-G.R. SP No. 63446, September 20,2001. Pertinent portions of said decision are hereby quoted as follows:

> "The law is clear in this case. As stated earlier, the granting by private establishments of 20% discount to senior citizens entitles them to "claim the cost as tax credit". Any interpretation substituting the phrase "tax credit" to "deduction from gross income tax" is unwarranted. Tax deduction and tax credit have different connotations and application. In the former, the taxes are deducted from the gross income in computing the taxable income, while in the latter, the taxes are deducted from the income tax itself. In other words, a tax credit entitles a corporation or establishment to deduct directly from the income tax due the cost of the 20% sales discount given to senior citizens; while a deduction from "gross income" merely entitles the establishment or corporation to deduct the cost of the 20% sales discount given to senior citizens after arriving at the "gross sales less returns, discounts and allowances and costs of goods sold."
>
> The construction given by petitioner in Revenue Regulations No. 2-94 issued to implement section 4 (a) of R.A. No. 7432 which provides that the 20% discount granted to senior citizens by private establishments shall be "deducted from their gross income" is clearly beyond the meaning of the phrase "tax credit". Hence, there being an obvious dichotomy between the two phrases, sections 2(i) and 4 of Revenue Regulations No. 2-94 cannot be given effect."

Further, as correctly pointed out by petitioner in its memorandum (CTA records, pp. 140-155), the deliberations of the Bicameral Conference Committee Meeting on Social Justice held on February 5, 1992 which finalized the contents of Republic Act No. 7432 clearly show that the real intent of the lawmakers was to treat the sales discounts to senior citizens as tax credit rather than as deductions from gross income, thus:

> "THE CHAIRMAN, (Rep. Unico). By the way, before that ano, about deductions from taxable income. I think we incorporated there a provision na – on the responsibility of the private hospitals and drugstores, hindi ba?
>
> SEN. ANGARA. O, o.

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THE CHAIRMAN (Rep. Unico). So, I think we have to put in also a provision here about the deductions from taxable income of that private hospitals, di ba ganon 'yan?

REP. AQUINO. Section 11 sa atin ano?

THE CHAIRMAN, (Rep. Unico).

Puwede na. Yung about the private hospitals. Yung isiningit natin?

MS. ADVENTO. Singit na po ba 'yung 15% on credit . . . (inaudible/did not use microphone).

SEN. ANGARA. Hindi pa, hindi pa.

THE CHAIRMAN, (Rep. Unico) Ah, 'di pa ba naisama natin?

SEN. ANGARA. O, o. You want to insert that?

THE CHAIRMAN (Rep. Unico). Yung ang proposal ni Senator Shahani, e.

SEN. ANGARA. . . . in the case of private hospitals . . . they got the grant of 15% discount, provided that, the private hospitals can claim the expense as a tax credit.

REP. AQUINO. Yah . . . could be allowed as deductions in the perpetrations of . . . (inaudible) income . . .

SEN. ANGARA. I-tax credit na lang natin para walang cash-out ano?

REP. AQUINO O, o, tax credit, Tama, Okay. Hospitals ba o lahat ng establishments na covered?

THE CHAIRMAN. (Rep. Unico) Sa kuwan lang 'yon, as private hospitals lang.

REP. AQUINO. Ano ba 'yung establishments na covered?

SEN. ANGARA. Restaurant. . lodging houses, recreation centers.

REP. AQUINO. All establishments covered siguro?

SEN. ANGARA. From all establishments. Alisin na natin 'yung kuwan kung ganon. Can we go back to Section 4 ha?

REP. AQUINO. Oho.

SEN. ANGARA. Letter A. To capture that thought, we'll say the grant of 20% discount from all establishments et. cetera, et cetera, provided that said establishments – provided that private establishments may claim the cost as a tax credit. Ganon ba 'yon?

REP. AQUINO. Yah.

SEN. ANGARA. Dahil kung government, they don't need to claim it.

THE CHAIRMAN. (Rep. Unico). Tax Credit.

SEN. ANGARA. As a tax credit rather than as kuwan – deduction, Okay.

REP. AQUINO. Okay.

SEN. ANGARA. Sige, Okay. Di, subject to style na lang sa letter A."
(pp. 22-24 underscoring supplied)

It is also significant to note that in the case of **Central Luzon Drug Corporation vs. Commissioner of Internal Revenue**, *supra*, the Court of Appeals ruled that the full amount and not only the cost of the 20% sales discounts to senior citizens shall be the basis of the tax credit, thus:

> "Lastly, the concept of tax credit as just compensation, leads us to conclude that the term cost under Sec. 4(a) of R.A. 7432 refers to cost of acquisition, not the cost of medicines sold to senior citizens, which was already reduced by 20%. Just compensation is the full and fair equivalent of the property taken from the private owner by expropriator. It is intended to fully indemnify the owner for the loss sustained. x x x Clearly, the cost of medicines sold to senior citizens, which is already discounted, does not come close to the full and fair equivalent of the property taken. It should not be the basis of the tax credit."

Having settled the legal issue, We shall now proceed to the factual aspect of the case. Hence, at this point, what is left for Us to determine is whether or not petitioner was able to substantiate its claim by documentary evidence.

To prove the fact of overpayment of income tax, petitioner must be able to establish the following:

1. it actually deducted the claimed amount of 20% sales discounts to senior citizens from its gross sales (income) in computing its income tax due for 1995;

2. it actually paid the corresponding amount of income tax due for 1995 as a result of the deduction of the claimed 20% sales discounts to senior citizens from its gross sales (income); and

3. the claimed amount of 20% sales discounts to senior citizens is duly supported by cash slips/cash register tape receipts *(Mercury Drug Corporation vs Commissioner of Internal Revenue, supra.)*

A circumspect study of the records would reveal that petitioner actually deducted from its 1997 gross sales only the amount of P956,853.36 *(Exhibit B-1)* out of the claimed 20% sales discounts to senior citizens of P1,052,539.00 resulting to a 1997 net sales of P108,693,107.00 *(Exhibit D-5).* The amount of P 108,693,107.00 is indicated in petitioner's 1997 audited financial statements as "Sales, Net" *(Exhibit C-1a)* and in Section C, Schedule 1 of its 1997 annual income tax return as "Gross Sales During The Year" *(Exhibit D-5).* As a result of said deduction, petitioner's 1997 income tax return showed a taxable income of P13,886,708.00 with the corresponding income tax due of P4,860,348.00, which was offset against the 1997 creditable taxes withheld of P4,237,187.48 and a final payment of P 623,160.52 *(Exhibit D-3).*

The auditing firm, Vicente E. Reyes & Associates, through its Partner, Mr. Rene Reyes, was commissioned by this Court pursuant to CTA Circular 1-95, as amended, to verify petitioner's claim for refund. The report prepared by Mr. Rene R. Reyes *(Exhibit J)* would reveal that out of the claimed 20% discounts to senior citizens for 1997 of

P1,052,539.00, only the amount of P1,050,855.78 *(Exhibit J-1)* was properly supported by cash slips.

Upon review of petitioner's "Summary of Cash Slips/Sales Discounts Granted to Senior Citizens for the year 1997" *(Pre-marked Exhibit L)* and the supporting cash slips *(Pre-Marked as Exhibit K with the cash slip numbers as sub-markings)*. We found the said report to be in order.

In computing petitioner's 1997 overpaid income tax, the total 20% sales discounts to senior citizens of P956,853.36 previously deducted by petitioner from its gross sales shall be added back to its net sales of P108,693,107.00, the reason being that the 20% sales discounts to senior citizens is no longer to be treated as deduction from gross income but rather as tax credit. Since the total substantiated 20% sales discounts amounting to P1,050,855.78 is inclusive of 10% value-added tax (VAT), it is necessary to exclude first the 10% VAT of P95,532.34 to arrive at petitioner's allowable tax credit. This resulted to the net amount of P955,323.44.

Therefore, a re-computation of petitioner's 1997 income tax liability using the figure P955,323.44 representing 20% sales discounts to senior citizens as tax credit will result to an income tax overpayment of P 620,424.96, computed as follows:

Net Sales			P 108,693,107.00
Add:	20% Sales Discount to Senior Citizens		956,853.36
Gross Sales			P 109,649,960.36
Less:	Cost of Sales		
	Merchandise inventory, beginning	P 11,937,299.00	
	Purchases	100,486,273.00	
	Total merchandise available for sale	P 112,423,572.00	
	Less: Merchandise inventory, end	13,555,792.00	98,867,780.00
Gross Profit			P 10,782,180.36
Add:	Miscellaneous Income		97,549,522.00
Total Income			P 108,331,702.36
Less:	Operating Expenses		21,091,724.00

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Net Income before Income Tax			P 87,239,978.36
Less: Income subjected to Final Tax			72,396,417.00
Net Taxable Income			P 14,843,561.36
Income Tax Due			P 5,195,246.48
Less: Tax Credits/Payments			
1.) 1997 Creditable taxes withheld	P	4,237,187.48	
2.) Final payment per ITR		623,160.52	
3.) 20% Sales discounts to senior citizens		955,323.44	5,815,671.44
Income Tax Refundable			P 620,424.96

WHEREFORE, in the light of the foregoing, the instant Petition for Review is **PARTIALLY GRANTED.** Respondent is hereby **ORDERED** to **ISSUE A TAX CREDIT CERTIFICATE** in favor of the petitioner in the reduced amount of P620,424.96 representing overpaid corporate income tax for taxable year 1997.

SO ORDERED.

Juanito C. Castaneda, Jr.
JUANITO C. CASTANEDA, JR.
Associate Judge

I CONCUR:

ERNESTO D. ACOSTA
Presiding Judge

CERTIFICATION

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

ERNESTO D. ACOSTA
Presiding Judge

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