REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

THIRD DIVISION

REPUBLIC CEMENT CORPORATION (as surviving corporation in a merger involving FR CEMENT CORPORATION),
Petitioner,

-versus-

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

CTA Case No. 7114

Members:

BAUTISTA, Chairperson
PALANCA-ENRIQUEZ, and
COTANGCO-MANALASTAS, *JJ.*

Promulgated:

MAR 17 2011
ABFernando 11:20 a.m.

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DECISION

COTANGCO-MANALASTAS, *J.:*

This is a Petition for Review filed on December 23, 2004 by Republic Cement Corporation (petitioner), pursuant to Section 7 of Republic Act No. 1125, as amended by Republic Act No. 9282, to review by appeal the Final Decision on Disputed Assessment dated December 16, 2004[1] of the Commissioner of Internal Revenue (respondent), which denied in part petitioner's administrative protest[2] filed on April 1, 2004 of the deficiency tax assessment, in the aggregate amount of P130,451,244.45, representing alleged deficiency income tax and withholding of final VAT, with interest and compromise penalties thereon for taxable year 1999.

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[1] Exhibit "E".
[2] Exhibit "C".

THE FACTS

The facts of the case, based on joint stipulations, judicial admission, and evidence on record, are as follows:

Petitioner FR Cement Corporation is a corporation duly organized and existing under the laws of the Philippines. It is engaged in the manufacture and distribution of cement, concrete aggregates and concrete products generally for the building and construction industry, and to carry on all businesses incident thereto or connected therewith.[3]

Respondent is the duly appointed Commissioner of the Bureau of Internal Revenue (BIR) who holds office at the BIR National Office Building, Agham Road, Diliman, Quezon City.

Petitioner filed its 1999 Annual Income Tax Return (ITR) on April 17, 2000 with the BIR Revenue District Office (RDO) No. 121, Excise Taxpayers Division in accordance with Section 77 of the National Internal Revenue Code (NIRC) of 1997.[4] Petitioner's Annual ITR for taxable year ended December 31, 1999 disclosed a net operating loss of P183,936,519.00.[5]

Petitioner filed its Quarterly Value-added Tax Returns for taxable year 1999 on the following dates: [6]

PERIOD	DATE OF FILING
1st Quarter	April 23, 1999
2nd Quarter	July 26, 1999
3rd Quarter	October 25, 1999
4th Quarter	January 25, 2000

[3] Pars. 1 and 4, Stipulation of Facts, Joint Stipulation of Facts and Issues (JSFI), docket, pp. 122-123.
[4] Exhibit "L"; Par. 25, Stipulation of Facts, JSFI, docket, p. 128.
[5] Exhibit "L-2"; Par. 28, Stipulation of Facts, JSFI, docket, p. 128.
[6] Par. 27, Stipulation of Facts, JSFI, docket, p. 128.

For taxable years 2000, 2001, and 2002, petitioner filed its Annual ITRs on the following dates:[7]

TAXABLE YEAR	DATE OF FILING
2000	April 18, 2001
2001	April 15, 2002
2002	April 15, 2003

Petitioner received a Letter of Authority No. 00003024 dated August 8, 2000 from the BIR, authorizing the examination of petitioner's books of accounts and other financial records for all internal revenue taxes for taxable year ended December 31, 1999.[8]

Petitioner executed a "Waiver of the Defense of Prescription Under the Statute of Limitations of the National Internal Revenue Code" (the "First Waiver") on December 19, without indicating the year it was signed by the taxpayer[9] but appears to be notarized on January 7, 2003.

On April 22, 2003, petitioner received a Preliminary Assessment Notice dated March 3, 2003 for alleged deficiency taxes pertaining to taxable year ended December 31, 1999.[10]

Subsequently, petitioner was made to execute five (5) other waivers on May 6, 2003 (the "Second Waiver")[11], August 26, 2003 (the "Third Waiver")[12], October 15, 2003 (the "Fourth Waiver")[13], November 11, 2003 (the "Fifth Waiver")[14], and January 6, 2004 (the "Sixth Waiver")[15], purportedly to afford respondent more time to

[7] Exhibits "M", "N", "N-2", and "O".
[8] Par. 5, Stipulation of Facts, JSFI, docket, p. 123.
[9] Exhibit "F"; Par. 6, Stipulation of Facts, JSFI, docket, p. 123.
[10] Exhibit "A".
[11] Exhibit "G".
[12] Exhibit "H".
[13] Exhibit "I".
[14] Exhibit "J".
[15] Exhibit "K".

assess and collect taxes beyond the prescriptive period provided under the NIRC of 1997.

On March 3, 2004, petitioner received from respondent Assessment Notice Nos. IT-99-00049, WFVAT-99-00001, and WTC-99-00020, together with the accompanying Formal Letter of Demand, all dated February 18, 2004 for alleged deficiency income tax, withholding of final value-added tax, and withholding tax on compensation for taxable year ended December 31, 1999 in the aggregate amount of P450,373,870.86, inclusive of interest and compromise penalties.[16]

Based on the said Assessment Notices, petitioner is liable for deficiency income tax of P422,754,163.08, withholding of final VAT of P27,614,045.70, and withholding tax on compensation in the amount of P5,662.08, inclusive of interests and compromise penalties, detailed as follows:[17]

Deficiency Income Tax	
Tax Due	P 238,372,145.64
Add: Interest	184,357,017.44
Compromise Penalty	25,000.00
TOTAL AMOUNT DUE	P 422,754,163.08
Deficiency Withholding of Final VAT	
Tax Due	P 15,177,162.34
Add: Interest	12,411,883.36
Compromise Penalty	25,000.00
TOTAL AMOUNT DUE	P 27,614,045.70
Deficiency Withholding Tax on Compensation	
Tax Due	P 2,564.68
Add: Interest	2,097.40
Compromise Penalty	1,000.00
TOTAL AMOUNT DUE	P 5,662.08

On April 1, 2004, petitioner filed an administrative protest on the ground that the assessments are without legal and factual bases.[18]

[16] Exhibits "B" to "B-3"; Par. 9, Stipulation of Facts, JSFI, docket, pp. 123-124.
[17] Exhibits "B-1" to "B-3"; Par. 10, Stipulation of Facts, JSFI, docket, p. 124.
[18] Exhibit "C"; Par. 11, Stipulation of Facts, JSFI, docket, p. 124.

On December 22, 2004, petitioner received from respondent a Final Decision on Disputed Assessment, partially granting the protest of petitioner, together with Assessment Notice Nos. IT-99-00067, WFVAT-99-00044, and WTC-99-00012, all dated December 16, 2004.[19]

In the assessment of deficiency income tax, respondent disallowed the deduction from petitioner's gross income from the write-off of investment during taxable year 1999 for being unsubstantiated, and noted a discrepancy in the volume of cement bags produced in the Daily Operation Report and the Production Cost Summary of petitioner for taxable year 1999. The aforesaid discrepancy was then concluded to have resulted in an under-declaration of income in the amount P4,953,047.36, after considering the average selling price and unit cost per bag of cement.[20]

Respondent also assessed petitioner of deficiency income tax pertaining to the clinker sales for taxable year 1999 in the amount of P34,293,759.25 on the assumption that clinker sales are not covered by petitioner's Income Tax Holiday in 1999, and that a correcting entry in the amount of P44,243,824.52 in relation to the purported disposal of heavy equipment in 1998 is not a deductible expense but should have been charged to Retained Earnings in 1999. Respondent disallowed deduction from petitioner's gross income in 1999 of various payments to suppliers of goods and services amounting to P63,705,446.21 that were allegedly not subjected to withholding tax. Respondent also disallowed deduction from petitioner's gross income in the amount of P2,467,706.25, representing depreciation expense

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[19] Exhibits "E" to "E-3"; Par. 12, Stipulation of Facts, JSFI, docket, pp. 124.
[20] Pars. 17, 18, and 19, Stipulation of Facts, JSFI, docket, p. 127.

corresponding to payments made to non-resident foreign corporations, which were charged to property account but were not subjected to final withholding tax.[21]

Respondent alleged that petitioner failed to withhold ten percent (10%) VAT on its payments to non-resident foreign corporations amounting to P151,771,623.25, broken down as follows:[22]

PAYMENTS	AMOUNT
Management fee (royalty)	P 3,709,248.00
Retention and Service of Elex Engineers	12,663,679.57
Krupp Polysius Service Contract	115,064,153.53
BMH Claudius Engineers	8,516,179.13
Retention and Service Fee of Mr. Jadgmann	6,840,442.64
BMH Claudius Engineers	4,977,920.38
TOTAL	**P 151,771,623.25**

In the Final Decision and the revised Assessment Notices, respondent assessed petitioner of deficiency income tax of P100,021,835.16, withholding of final VAT of P30,429,409.29, and withholding tax on compensation in the amount of P6,137.82, inclusive of interest and compromise penalties for taxable year 1999, computed as follows:[23]

Deficiency Income Tax	
Tax Due	P 51,050,048.58
Add: Interest	48,946,786.58
Compromise Penalty	25,000.00
TOTAL AMOUNT DUE	P100,021,835.16
Deficiency Withholding of Final VAT	
Tax Due	P 15,177,162.33
Add: Interest	15,227,246.96
Compromise Penalty	25,000.00
TOTAL AMOUNT DUE	P 30,429,409.29
Deficiency Withholding Tax on Compensation	
Tax Due	P 2,564.68
Add: Interest	2,573.14
Compromise Penalty	1,000.00
TOTAL AMOUNT DUE	P 6,137.82

[21] Pars. 20, 21, 22, and 23, Stipulation of Facts, JSFI, docket, p. 127.
[22] Par. 24, Stipulation of Facts, JSFI, docket, pp. 127-128.
[23] Exhibits "E" to "E-3".

Consequently, upon receipt of the above-mentioned Final Decision on Disputed Assessment[24] on December 22, 2004, petitioner filed the instant Petition for Review on December 23, 2004, praying that the deficiency income tax and withholding of final VAT in the amounts of P100,021,835.16 and P30,429,409.29, respectively, inclusive of interest and compromise penalties, for taxable year 1999 be declared devoid of factual and legal bases, and that the above-mentioned assessments be withdrawn and cancelled.

In his Answer[25] filed on February 21, 2005, respondent interposed the following Special and Affirmative defenses:

"SPECIAL AND AFFIRMATIVE DEFENSES

3. The right of the government to asses has not prescribed, as petitioner executed valid waivers of the statute of limitations extending the prescriptive period to assess pursuant to Section 222 of the Tax Code.

INCOME TAX

4. Investment in stock amounting to P5,033,333.33 was written off and deducted as expense. However, petitioner failed to meet the deductibility requirements pursuant to Section 34(A)(1)(b) of the NIRC, hence disallowed as expense.

5. There was a discrepancy in the taxable sales per investigation as against taxable sales per income tax return in the amount of P34,293,759.25 representing clinker sales which is not included for purposes of Income Tax Holiday, hence, assessed as income pursuant to Section 32 of the Tax Code.

6. Comparison of production in cement bags per Daily Operation Report versus Production Cost Summary resulted to a discrepancy in the number of cement bags. Since the discrepancy was no longer included in the inventory, it was considered sold. The number of cement bags multiplied by average selling price minus the cost resulted to unreported income of P4,953,047.36, hence, assessed pursuant to Section 32 of the Tax Code.

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[24] Exhibit "E".
[25] Answer, docket, pp. 80-84.

7. Correcting entry in relation to the disposal of heavy equipment in 1998 amounting to P44,243,620,886.13 was charged to Other Expense on Management Operation (Depreciation Expense) instead of Retained Earnings. Verification, likewise, disclosed that the entry made was to correct the debit balance of accumulated depreciation, hence, the disallowance pursuant to Section 34(A)(1)(b) of the Tax Code.

8. Income payments amounting to P63,705,446.21, which were not subjected to withholding tax under Revenue Regulations 2-98, were disallowed as expense pursuant to Section 34(K) of the Tax Code.

9. Payments for services to non-resident foreign corporation amounting to P151,771,623.25 were not subjected to final tax but were charged to property account, hence, the disallowance of depreciation expense pertaining to the months not covered by ITH in the amount of P2,467,706.25 pursuant to Section 34(K) of the Tax Code.

WITHHOLDING OF FINAL VAT

10. Investigation disclosed that there were payments for services to non-resident foreign corporations which were not subjected to final withholding VAT. Petitioner failed to submit proof that the payments to Krupp Polysius and Elex Engineers were for 1998 transactions, hence, the assessment in the amount of P151,771,623.25 pursuant to Section 114 (C) of the Tax Code and Revenue Regulations No. 7-95.

WITHHOLDING TAX ON COMPENSATION

11. Comparison of withholding tax due per Alphalist of P16,962,271.66 versus Remittance per Returns of P16,959,706.98 resulted to a discrepancy of P2,564.68. Petitioner failed to submit proof of remittance of said amounts, hence, the assessment pursuant to Sections 80 and 81 of the Tax Code.

12. The assessment was issued in accordance with law and regulations.

13. All presumptions are in favor of the correctness of tax assessments."

During trial, petitioner presented as witnesses the following: Ms. Amie Ajero[26], Mr. Gilbert Q. Aresta[27], Mr. Emmanuel Y. Mendoza[28], and Mr. Rodel N.

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[26] Minutes, docket, pp. 136, 155, 158, 218, 219, 342, 350, and 352.
[27] Minutes, docket, pp. 146 and 147.
[28] Minutes, docket, pp. 164 and 217.

Binuya[29]. Thereafter, petitioner filed its Formal Offer of Evidence[30] on March 3, 2008, submitting Exhibits "A" to "O", and "T" to "MM", inclusive of sub-markings.

On March 18, 2008, petitioner filed a Manifestation and Omnibus Motion[31] praying, among others, for the reduction of the amount of bond equivalent only to one and one half times the amount of P30,429,409.29, the remaining deficiency final withholding VAT being collected or in the total amount of P45,644,113.93, in light of petitioner's availment of the tax amnesty program on March 6, 2008; and to order respondent to reflect in the BIR's records the closure and termination of the deficiency income tax assessment pursuant to Republic Act (R.A.) No. 9480 by issuing an Authority to Cancel Assessment or any other document showing the same.

On June 23, 2008, petitioner filed a Supplement [To Petition for Review dated December 22, 2004 Pursuant to Sec. 6, Rule 10 of the 1997 Rules of Civil Procedure][32]. In the said Supplement, petitioner alleged that on March 6, 2008, it availed of the tax amnesty program pursuant to R.A. No. 9480 and paid the amnesty tax amounting to P7,162,084.00.[33] Thus, petitioner averred that it is immune from the payment of taxes and the appurtenant civil, criminal or administrative penalties under the NIRC of 1997, particularly, the assessment for deficiency income tax for the year 1999, in the amount of P100,021,835.16. Petitioner further asserted that what remains pending for the resolution of this Court is the issue of deficiency withholding of final VAT assessment in the amount of P30,429,409.29.

[29] Minutes, docket, p. 269.
[30] Docket, pp. 380-407.
[31] Docket, pp. 408-413.
[32] Docket, pp. 484–491.
[33] Annex "A", Supplement [To Petition for Review dated December 22, 2004 Pursuant to Sec. 6, Rule 10 of the 1997 Rules of Civil Procedure], docket, p. 492.

In the Resolution[34] dated October 29, 2008, this Court resolved among others, that petitioner had duly complied with the provisions of R.A. No. 9480 and thereby noted and granted petitioner's Manifestation and Motion filed on March 18, 2008. Consequently, the instant Petition for Review was deemed withdrawn as regards the issue on petitioner's deficiency income tax and the case covering the same was considered closed and terminated, subject to the provisions of R.A. No. 9480. However, petitioner's deficiency withholding of final VAT and deficiency withholding tax on compensation assessments, which are not covered by the law, stays.

In the Resolution[35] dated December 4, 2008, this Court resolved among others, the admissibility of petitioner's exhibits in its Formal Offer of Evidence[36] filed on March 3, 2008. On December 22, 2008, petitioner filed a Motion[37] praying for the reconsideration of the Resolution dated December 4, 2008 and the admission of Exhibits "T-3","BB", "LL", "LL-1", and "MM", which this Court granted in a Resolution[38] dated February 5, 2009.

On February 23, 2009, petitioner filed a Motion to Amend Caption[39] of this case from "FR Cement Corporation vs. Commissioner of Internal Revenue" to "Republic Cement Corporation (as surviving corporation in a merger involving FR Cement Corporation) vs. Commissioner of Internal Revenue". In the Resolution[40] dated March 16, 2009, this Court granted the above motion and the caption of the

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[34] Docket, pp. 622-625.
[35] Docket, pp. 686-689.
[36] Docket, pp. 380-407.
[37] Docket, pp. 691-701.
[38] Docket, pp. 704-705.
[39] Docket, pp. 709-710.
[40] Docket, pp. 729-730.

case was then changed to "Republic Cement Corporation (as surviving corporation in a merger involving FR Cement Corporation) vs. Commissioner of Internal Revenue."

On the other hand, on September 15, 2009, respondent presented as lone witness Mr. Avelino P. Domaoan, Jr.[41] Thereafter, on October 27, 2009 respondent filed his Formal Offer of Evidence[42], submitting Exhibits "1" to "8", inclusive of sub-markings; which this Court admitted in a Resolution[43] dated January 5, 2010.

The case was submitted for decision on April 6, 2010, taking into consideration the Memorandum of petitioner filed on March 15, 2010 and Reply-Memorandum filed on April 5, 2010; and respondent's Memorandum filed on March 19, 2010.

The following are the parties' jointly stipulated issues[44] submitted for this Court's consideration:

> "1. Whether or not the right of the Government to assess deficiency taxes for taxable year ended December 31, 1999 (sic) has already prescribed.
>
> 2. Assuming the right of the Government to assess deficiency taxes for taxable year ended December 31, 1999 has not yet prescribed, whether or not the assessment notices should be cancelled for lack of factual and legal bases.
>
> 3. Whether or not petitioner is liable to pay the amount of P130,451,244.45 as deficiency income tax and withholding of final VAT for taxable year 1999."

In view of petitioner's availment of tax amnesty, this Court's evaluation will now be limited to the remaining issue which pertains to the validity of respondent's assessment of deficiency withholding of final VAT for taxable year 1999.

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[41] Minutes, docket, pp. 782 and 783.
[42] Docket, pp. 785-788.
[43] Docket, pp. 802-803.
[44] Docket, p. 129.

THE COURT'S RULING

Petitioner alleges that the assessment of deficiency withholding of final VAT for taxable year 1999 is barred by prescription, claiming that the applicable period of prescription is three (3) years from the time a tax return is filed within which to assess deficiency taxes, citing Section 203 of the NIRC of 1997. Petitioner claims that from its date of filing of the VAT return on January 25, 2000, respondent had until January 25, 2003 within which to assess petitioner for deficiency final withholding VAT. Petitioner asserts that the Assessment Notice for deficiency final withholding VAT for taxable year 1999 was received by petitioner only on March 3, 2004, beyond the three-year period prescribed by law for the assessment and collection of taxes.[45]

Petitioner next argues that the waivers it executed are not valid since they did not comply with the requisites and formalities of a valid waiver. Petitioner concludes that the waivers did not have the effect of extending the three-year prescriptive period and the right of the government to assess deficiency income tax and withholding of final VAT for taxable year ending December 31, 1999 is already barred by the statute of limitations.[46]

Respondent, on the other hand, maintains that the right of the government to assess has not prescribed as petitioner executed valid waivers of the statute of limitations extending the prescriptive period to assess pursuant to Section 222 of the Tax Code. In his Answer, respondent claims that there were payments for services to non-resident foreign corporations which were not subjected to final withholding VAT and that petitioner failed to submit proof that the payments to Krupp Polysius and

[45] Pars. 31, 32, 33, and 34, Memorandum of petitioner, docket, pp. 834-835.
[46] Pars. 38 and 55, Memorandum of petitioner, docket, pp. 837 and 847.

Elex Engineers were for 1998 transactions; hence, the assessment was sustained pursuant to Section 114(C) of the NIRC of 1997 and Revenue Regulations No. 7-95.[47]

The Court agrees with respondent.

Section 203 of the NIRC of 1997 provides for a three (3)-year period to assess an internal revenue tax, to wit:

> "SEC. 203. *Period of Limitation Upon Assessment and Collection.* - 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."

In relation thereto, Section 222 of the NIRC of 1997 provides for exceptions to the period of limitations on the assessment and collection of taxes, *viz*:

> "SEC. 222. *Exceptions as to Period of Limitation of Assessment and Collection of Taxes.* –
>
> (a) In the case of a false or fraudulent return with intent to evade tax or **of failure to file a return, the tax may be assessed, or a proceeding in court for the collection of such tax may be filed without assessment, at any time within ten (10) years after the discovery of** the falsity, fraud or **omission**: *Provided*, That in a fraud assessment which has become final and executory, the fact of fraud shall be judicially taken cognizance of in the civil or criminal action for the collection thereof.
>
> (b) If before the expiration of the time prescribed in Section 203 for the assessment of the tax, both the Commissioner and the taxpayer have agreed in writing to its assessment after such time, the tax may be assessed within the period agreed upon. The period so agreed upon may be extended by subsequent written agreement made before the expiration of the period previously agreed upon." *(Emphasis supplied)*

In the instant case, records show that petitioner failed to file a return for the taxes being assessed against it. No evidence was presented by petitioner to prove that

[47] Answer, docket, pp. 81-82.

it duly filed corresponding tax returns for the subject deficiency withholding of final VAT.

Thus, the Court finds that petitioner's deficiency withholding of final VAT may be assessed or a proceeding in this court for the collection of such tax may be filed without assessment, at any time within ten (10) years after the discovery of the said omission. Accordingly, respondent's right to assess petitioner's deficiency withholding of final VAT for taxable year 1999 has not prescribed when he issued on March 3, 2004 the Formal Letter of Demand[48] and Assessment Notice.[49] In view of the applicability of the 10-year prescriptive period, the resolution of the issue pertaining to the validity of waivers executed by petitioner is no longer necessary.

Respondent's investigation disclosed that there were payments of services to non-resident foreign corporation which were not subjected to the payment of final withholding VAT prescribed under Section 114(C) of the NIRC of 1997 and under Section 4.102 of Revenue Regulations No. 7-95, amounting to P151,771,623.25[50], broken down as follows:

A. Management fee (royalty)	P 3,709,248.00
B. Retention and Service of Elex Engineers	12,663,679.57
C. Krupp Polysius Service Contract	115,064,153.53
D. BMH Claudius Engineers	8,516,179.13
E. Retention and Service Fee of Mr. Jadgmann	6,840,442.64
F. BMH Claudius Engineers	4,977,920.38
TOTAL	**P 151,771,623.25**

Pursuant to Section 114(C) of the NIRC of 1997, petitioner is required to withhold ten percent (10%) creditable VAT on its payments of services to non-resident foreign corporation, to wit:

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[48] Exhibit "B".
[49] Exhibit "B-2".
[50] Per Detailed Computations attached to Exhibit "E".

> "(C) *Withholding of Creditable Value-added Tax.* – The Government or any of its political subdivisions, instrumentalities or agencies, including government-owned or -controlled corporations (GOCCs) shall, before making payment on account of each purchase of goods from sellers and services rendered by contractors which are subject to the value-added tax imposed in Sections 106 and 108 of this Code, deduct and withhold the value-added tax due at the rate of three percent (3%) of the gross payment for the purchase of goods and six percent (6%) on gross receipts for services rendered by contractors on every sale or installment payment which shall be creditable against the value-added tax liability of the seller or contractor : *Provided, however,* That in the case of government public works contractors, the withholding rate shall be eight and one-half percent (8.5%): *Provided, further,* That **the payment for lease or use of properties or property rights to nonresident owners shall be subject to ten percent (10%) withholding tax at the time of payment. For this purpose, the payor or person in control of the payment shall be considered as the withholding agent.**
>
> **The value-added tax withheld under this Section shall be remitted within ten (10) days following the end of the month the withholding was made.**" (*Emphasis supplied*)

It must be noted that the subject deficiency tax was erroneously indicated by respondent as "WT of Final VAT" in his Final Decision on Disputed Assessment dated December 16, 2004. The withholding VAT referred to under Section 114(C) of the NIRC of 1997 as afore-quoted, is creditable and not final in nature. It was only when R.A. No. 9337[51] became effective on November 1, 2005 that the withholding VAT under Section 114(C) became a final tax.

A. Management Fee (Royalty) – P3,709,248.00

Upon comparison of petitioner's Management Fee (Royalty) as reflected in its income tax return/financial statements *vis-à-vis* the amount shown in its withholding tax return (BIR Form No. 1601), respondent found that Management Fee (Royalty) amounting to P3,709,248.00 was not subjected to creditable withholding VAT, computed as follows:[52]

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[51] An Act Amending Sections 27, 28, 34, 106, 107, 108, 109, 110, 111, 112, 113, 114, 116, 117, 119, 121, 148, 151, 236, 237 and 288 of the National Internal Revenue Code of 1997, as Amended, and for Other Purposes.

[52] Exhibit "A", Schedule 5.

Management Fee	
Per ITR/FS	P 44,667,775.00
Per W/Tax Return 1601	40,958,527.00
Discrepancy	**P 3,709,248.00**

Petitioner availed of the Voluntary Assessment and Abatement Program (VAAP) and paid the 10% creditable withholding VAT of P370,924.80 on the Management Fee (Royalty) discrepancy of P3,709,248.00 on October 31, 2003.[53] Therefore, respondent's inclusion of this item in the total deficiency final withholding VAT of P30,429,409.29 reflected per Final Decision on Disputed Assessment dated December 16, 2004 is erroneous.

B. <u>Retention and Service of Elex Engineers – P12,663,679.57</u>

Petitioner asserts that Journal Voucher No. 070125[54] merely shows a reclassification entry from "Prepaid Importation Charges" to a temporary account "Factory Ledger", which means that the project has been assessed to be completed and operational, and the fixed assets were recorded in the books of the plant office in Teresa, Rizal. This will be subsequently reclassified to the proper fixed account upon formally recording in the books at the principal office in Pasig.

The Court is not convinced since the said journal voucher and petitioner's allegations are unverifiable and self-serving, if not dubious, and can be contrived easily considering that no other supporting documents were presented before this Court, to prove that it was indeed capitalized. Hence, this document merits very little weight and respondent's assessment thereon is proper.

[53] BIR Records, pages 1599-1604.
[54] Exhibit "DD-92".

C. <u>Krupp Polysius Service Contract – P115,064,153.53</u>

Petitioner asserts that the amount of P115,064,153.53 represents the total expenses or payments incurred for the project from 1996 to 1998, which project was assessed to be complete and operational only in 1999. Such were not payments made to Krupp Polysius during taxable year 1999, which is the year covered in the subject assessments.

Petitioner explained that in long-term projects, such as the project involving the services of Krupp Polysius, it maintains a manual ledger which lists all expenses incurred for that particular project. To support its allegations, petitioner offered in evidence the said manual ledger[55] showing that all expenses were recorded under the account of Krupp Polysius from the start of construction in March 1996 until 1998. These expenses were purportedly charged to "Prepaid Importation Charges" at the time these were incurred. On the last two items of page 8 of Exhibit "DD-94", it was indicated that as of November 30, 1998, the total expenses incurred for the construction under Krupp Polysius amounted to P115,064,153.53. This was closed on July 31, 1999 through Journal Voucher No. 070191[56], with the following entry:

"Factory Ledger	P115,052,222.02	
Input Tax	11,931.51	
Prepaid Importation Charges		P115,064,153.53"

Thus, the said entry was merely a reclassification entry upon the completion of the project in 1999 and is not an entry on actual payment to Krupp Polysius in 1999.

Moreover, a portion of these payments includes expenses for the board and lodging, transportation, and other incidental expenses of employees of Krupp Polysius in the Philippines that were shouldered by petitioner and paid directly to domestic

[55] Exhibit "DD-94", consisting of 8 pages.
[56] Exhibit "DD-93".

corporations or business. The Court-commissioned Independent CPA[57] summarized the payments of P115,064,153.53 as follows:[58]

Payee	Nature of Payment	Annex (to Exhibit CC)	Amount
Ruby Lane Inn	Accomodation	B	P 308,868.19
Classic Travelhouse, Inc.	Agency Assistance	C	1,571,497.00
Las Brisas Hotel & Conference	Accomodation	D	135,451.70
TNT Express Worldwide	Services (shipment) Expenses	E	17,476.47
FR Cement	Liquidation	F	59,572.65
Various	Manual Ledger	G	7,118,167.21
Sub-Total			**P 9,211,033.22**
Equitable Bank per LC No. 96-0819 for Krupp Polysius	Services	H	105,853,120.31
TOTAL			**P115,064,153.53**

To prove that Las Brisas Resorts Corp., TNT Express Worldwide, and Classic Travelhouse Inc. were indeed domestic corporations registered with the Securities and Exchange Commission (SEC), petitioner submitted in evidence their SEC Certification.[59] By virtue of their domestic incorporation, the payments to the above-mentioned corporations shall not be subjected to withholding of creditable VAT.

However, a perusal of the supporting documents for the P115,064,153.53 expenses indicates that only the amount of P67,612,146.89, as provided below, can be ascertained as payment to domestic corporations and were made from 1996 to 1998. *Ergo*, the unverified amount of P47,452,006.64 shall be subject to withholding of final VAT.

Payee	Annex (to Exhibit CC)	Amount
Antipolo Thrift Shop & General Merchandise	DD-17a	P 134,600.00
Classic Travelhouse Inc.	DD-18a	122,510.00
Classic Travelhouse Inc.	DD-18b	122,510.00

[57] Mr. Emmanuel Y. Mendoza, Partner of Mendoza Querido & Co.
[58] Exhibit "CC", page 5, docket, p. 172.
[59] Exhibits "FF", "FF-1" and "FF-2".

Classic Travelhouse Inc.	DD-18c	122,208.00
Classic Travelhouse Inc.	DD-18d	1,830.00
Classic Travelhouse Inc.	DD-19a	5,280.00
Classic Travelhouse Inc.	DD-20b	121,074.00
Classic Travelhouse Inc.	DD-20c	121,075.00
Classic Travelhouse Inc.	DD-20d	121,074.00
Classic Travelhouse Inc.	DD-20e	119,744.00
Classic Travelhouse Inc.	DD-22b	89,639.00
Classic Travelhouse Inc.	DD-23b	131,991.00
Classic Travelhouse Inc.	DD-24b	119,457.00
Classic Travelhouse Inc.	DD-25b	1,657.00
Classic Travelhouse Inc.	DD-25c	162,731.00
Classic Travelhouse Inc.	DD-26a	860.00
Classic Travelhouse Inc.	DD-27a	1,470.00
Classic Travelhouse Inc.	DD-27a	2,680.00
Classic Travelhouse Inc.	DD-29b	185,897.00
Las Brisas Resort Corp.	DD-30a	32,855.00
Las Brisas Resort Corp.	DD-31a	35,978.80
Las Brisas Resort Corp.	DD-32a	37,733.85
Las Brisas Resort Corp.	DD-33a	24,044.05
Las Brisas Resort Corp.	DD-33a	3,090.00
Las Brisas Resort Corp.	DD-34a	1,750.00
TNT Express Worldwide	DD-35a	1,537.00
TNT Express Worldwide	DD-36a	5,545.00
TNT Express Worldwide	DD-37a	10,394.47
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-42a	1,447,080.90
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-43a/b	1,199,195.52
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-44a	247,103.40
EBC Insurance Brokerage Inc.	DD-445a	52,259.62
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-48a	12,647,304.47
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-49a	2,529,675.26
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-50a	86,733.41
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-51a	810,562.33
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-52a	3,031,043.46
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-53a	6,221,415.25
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-54a	2,283,312.73
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-58	18,344,209.35
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-59a	2,269,509.60
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-60a	1,538,820.42
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-61a	1,583,410.91
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-62a	3,233,766.10
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-63a	257,862.51
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-64a	122,667.87
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-65a	614,813.47
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-66a	84,518.68
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-67a	340,207.40

Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-68a	652,823.44
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-70a	253,959.56
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-85a	2,186,817.89
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-86a	846,304.43
Equitable Bank per LC No. 96-0819 for Krupp Polysius	DD-87a	2,885,553.74
	TOTAL	**P 67,612,146.89**

D. BMH Claudius Engineers – P8,516,179.13

Based on the address indicated in the invoices, it appears that BMH Claudius Engineers is a non-resident foreign corporation and based in Germany, whose services were engaged by petitioner to oversee and supervise the reconstruction of its Teresa Plant. The supporting documents submitted before this Court reveal that out of the alleged payment of P8,516,179.13, only the amount P8,424,547.88 pertains to payment of services to BMH Claudius Engineers, and thus, must be subject to withholding of final VAT.

Invoice No.	Exhibit No.	Payment Date per Bank Debit Advice	Exhibit No.	Journal/Cash Voucher Date	Exhibit No.	Amount
0110670/2	DD-2b	10/5/1999	DD-2b	10/15/1999	DD-2	P 1,668,967.28
0518270/2	DD-3b	11/18/1999	DD-3a	11/22/1999	DD-3	746,034.84
0510708/0	DD-5b	10/15/1999	DD-5a			2,391,471.51
0504597/2	DD-6b			8/9/1999	DD-6	891,591.96
0504644/2	DD-7b			8/27/1999	DD-7	987,007.57
0492740/2	DD-9c			7/16/1999	DD-9	1,136,432.23
0504597/2	DD-10c			7/26/1999	DD-10	603,042.49
					TOTAL	**P8,424,547.88**

As ascertained by the Independent CPA, petitioner did not file nor remit the withholding VAT related to payments made to BMH Claudius Engineers; hence, respondent's assessment shall be upheld.

E. Retention and Service Fee of Mr. Jadgmann – P6,840,442.64

Records disclosed that Mr. Reinhard Jagdmann, BMH Commissioning Supervisor, is a non-resident individual engaged by petitioner to render engineering services for the construction of Packhouse & Cement Silo Project at petitioner's Teresa Plant.

The manual ledger under the name of Mr. Jagdmann disclosed the details of payments in the amount of P6,840,442.64 as follows:

Particulars	Annex (to Exhibit CC)	Amount
Bobcock Materials Handling (machinery & equipment 10% retention fee)	I	P6,612,115.51
Services of Mr. Jagdmann	I	44,727.60
Adjustment (additional due to forex)	I	183,599.53
TOTAL		**P6,840,442.64**

Petitioner alleged that the payment to Bobcock Materials Handling (BMH) represents payment of retention fee or part of the purchase price of the importation of machinery and equipment from BMH and was erroneously recorded as payments for services of Mr. Jagdmann, and should therefore not be treated as payment for services to Mr. Jagdmann in 1999. However, this Court is not convinced that the amount of P6,612,115.51 was really payment of retention fee for the purchase of machinery and equipment since petitioner presented in evidence only its journal voucher[60], which is considered as self-serving; and the invoices[61] and Import Entry and Internal Revenue Declarations[62] do not actually reflect the said retention value to corroborate the journal voucher. Even the Independent CPA was not able to validate the supporting documents on the payment of the retention fee of P6,612,115.51.

[60] Exhibit "DD-88".
[61] Exhibits "DD-88a1/2" to "DD-88c2/2".
[62] Exhibits "DD-88d" to "DD-88g".

As to the amount of P44,727.60, the same pertains to payment of services to Mr. Jagdmann, which is supported by the invoice[63] issued by BMH together with petitioner's journal voucher[64] to record such payment of services.

No additional supporting documents was made available for the amount of P183,599.53 representing additional charges on foreign exchange difference; thus, the findings of respondent that the total amount of P6,840,442.64, representing payment of services to Mr. Jagdmann, should be subject to withholding of creditable VAT shall be upheld.

F. <u>BMH Claudius Engineers – P4,977,920.38</u>

As found by the Independent CPA, BMH Claudius Engineers is a non-resident foreign corporation, based in Germany, whose services were engaged by petitioner for the erection and commissioning of Packhouse No. 3.

Petitioner explained that the journal voucher[65] upon which the assessment was based merely shows a reclassification entry from "Prepaid Importation Charges" to a fixed asset account, "PPE Expansion", and not the actual payment to BMH Claudius Engineers in 1999. Except for the journal voucher, petitioner did not submit any other supporting documents to prove that indeed the same amount is part of its "PPE Expansion" account. As a consequence, respondent's assessment thereon shall be upheld.

In sum, this Court finds that the assessment issued by respondent against petitioner covering deficiency creditable withholding VAT for taxable year 1999 must be upheld but with some modifications. The compromise penalty of P25,000.00 is

[63] Exhibit "DD-89a".
[64] Exhibit "DD-89".
[65] Exhibit DD-91.

cancelled there being no mutual agreement between the parties.[66] Likewise, the basic deficiency creditable withholding VAT is reduced from P15,177,162.33 to P8,035,859.71. However, a twenty-five percent (25%) surcharge in the amount of P2,008,964.93 is imposed pursuant to Section 248(A)(3) of the NIRC of 1997.

WHEREFORE, the instant Petition for Review is hereby **PARTIALLY GRANTED.** Accordingly, the assessment of deficiency creditable withholding VAT for taxable year 1999 is hereby **AFFIRMED** with some **MODIFICATIONS.** Accordingly, petitioner is hereby **ORDERED TO PAY** respondent the amount P10,044,824.64 inclusive of the twenty-five percent (25%) surcharge imposed under Section 248(A)(3) of the NIRC of 1997, as amended, computed as follows:

Taxable basis per return			P 40,958,527.00
Add:	Royalty payments to Non Resident Foreign Corporation – Sec. 114(C) NIRC		
	Retention and Service of Elex Engineers	P 12,663,679.57	
	Krupp Polysius Service Contract	47,452,006.64	
	BMH Claudius Engineers	8,424,547.88	
	Retention and Service Fee of Mr. Jadgmann	6,840,442.64	
	BMH Claudius Engineers	4,977,920.38	80,358,597.11
Taxable basis per Investigation			P121,317,124.11
Tax Due per Investigation			P12,131,712.41
Less:	Payments per Return		4,095,852.70
Deficiency Creditable Withholding VAT			P 8,035,859.71
Add:	25% Surcharge		2,008,964.93
Total Deficiency Creditable Withholding VAT			**P 10,044,824.64**

Likewise, petitioner is hereby **ORDERED TO PAY** (a) deficiency interest at the rate of twenty percent (20%) *per annum* on the basic deficiency creditable withholding VAT of P8,035,859.71 computed from January 25, 2000, until full payment thereof pursuant to Section 249(B) of the NIRC of 1997; and (b)

[66] *Commissioner of Internal Revenue vs. UST*, 104 Phil. 1062.

delinquency interest at the rate of twenty percent (20%) *per annum* on the total deficiency taxes of P10,044,824.64 and on the 20% deficiency interest which have accrued as afore-stated in (a), computed from December 22, 2004 until full payment thereof, pursuant to Section 249(C) of the NIRC of 1997.

SO ORDERED.

AMELIA R. COTANGCO-MANALASTAS
Associate Justice

WE CONCUR:

LOVELL R. BAUTISTA
Associate Justice

OLGA PALANCA-ENRIQUEZ
Associate Justice

ATTESTATION

I attest 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's Division.

LOVELL R. BAUTISTA
Associate Justice
Chairperson

CERTIFICATION

Pursuant to Article VIII, Section 13 of the Constitution and the Division Chairperson's Attestation, 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's Division.

ERNESTO D. ACOSTA
Presiding Justice