Library

REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

RIZAL MOTORS, INC.,
Petitioner,

versus

C.T.A. CASE NO. 1985

COMMISSIONER OF
INTERNAL REVENUE,
Respondent.

10/27/72

x - - - - - - - - - x

D E C I S I O N

This is an appeal from the decision of respondent assessing petitioner in the sum of ₱768,982.77, representing deficiency sales and advance sales taxes for the period from 1956 to 1959, inclusive of surcharges and compromise penalty.

Petitioner is a corporation duly organized and existing under and by virtue of the laws of the Philippines, with principal office at Canley Road, Pasig, Rizal. It is engaged in the assembly and sale of cars and trucks, and in the sale of spare parts.

Pursuant to Letter of Authority No. 1657 R, dated December 14, 1959, petitioner was investigated by Examiners Perfecto M. Valenzuela and Jose Fuentes for business tax purposes. In a memorandum for the Provincial Revenue Officer, Quezon City, dated

March 14, 1960, the examiners recommended that petitioner be assessed the sum of ₱1,284,695.74 and be summoned to an informal conference as it has signified the intention of contesting said proposed assessment.

On March 22, 1960, petitioner disputed the proposed assessment and requested cancellation and withdrawal of the same. A reinvestigation was conducted by Examiner Pablito J. Enano who recomputed the proposed tax liability of petitioner resulting in the reduction thereof and recommended to respondent that the case be referred to the Legal Department for evaluation. His recommendation was concurred in by the Chief, Investigation Division.

Subsequently, in a memorandum for the Provincial Revenue Officer, Quezon City, dated September 9, 1963, Examiner Perfecto M. Valenzuela recomputed the assessment against petitioner which amounted to ₱758,664.48, inclusive of surcharges and recommended that a letter of demand for the said amount be sent to petitioner.

In a letter dated February 11, 1964, respondent assessed petitioner in the sum of ₱768,982.77 for deficiency sales and advance sales taxes for the years 1956 to 1959, inclusive of surcharges and compromise penalty, summarized as follows:

Billing of Sales Tax as a Separate Item . . .	₱ 1,254.69
Billing of Advance Sales Tax	2,397.17
Tax Exempt Raw Materials . .	19,915.63
Deficiency Advance Sales Tax	1,255.42
Deficiency Sales Tax	734,159.86
TOTAL AMOUNT DUE & DEMANDABLE	₱ 758,982.77
Plus: Compromise Penalty. .	10,000.00
GRAND TOTAL	₱ 768,982.77

Petitioner wrote respondent a letter on June 30, 1964, protesting the assessment on the ground of prescription and/or that it was made without factual or legal basis, and requesting that the amounts of ₱19,915.63 and ₱734,159.86 be cancelled and withdrawn. In a letter dated January 15, 1969, respondent denied petitioner's request and reiterated the demand for the sum of ₱768,982.77.

We are going to deal with the various items subject of deficiency tax assessment in the order they are treated by respondent in his assessment dated February 11, 1964.

<u>Sales Tax Not Billed as Separate Item, ₱1,254.69</u> -

This amount of ₱1,254.69 allegedly represents 50% of the total amount of sales tax billed to a customer on April 30, 1959, which was not billed separately or itemized in the sales invoice, imposed by Section 184 of the Revenue Code, plus 25% surcharge prescribed under Section 183(a) of the same Code, computed as follows:

Sales tax billed to customer not itemized or billed separately in the invoice . .	₱2,007.50
Tax Due at 50% (Sec. 184) . .	₱1,003.75
Add: 25% surcharge	250.94
TOTAL AMOUNT DUE	₱1,254.69

Petitioner does not dispute its liability for deficiency sales tax in the amount of ₱1,003.75 but objects to the inclusion of 25% surcharge thereon, or ₱250.94, on the ground that it was not guilty of intentional violation of the law and the delay was not in the filing of the sales tax return but in the payment of deficiency due to reliance on a ruling of respondent allowing the billing of sales tax to customers with the mere notation of the words "tax included" as sufficient compliance of General Circulars Nos. 431 and 440 of the Bureau of Internal Revenue, citing in support thereof the case of Connell Bros. (Phil.) v. Coll. of Int. Rev., 9 SCRA 735.

On this point, respondent counters that the [illegible] in the Connell Bros. case has been set aside by the Supreme Court in the case of Republic v. Philippine Bank of Commerce, 34 SCRA 361.

We disagree with the stand advocated by respondent.

The Philippine Bank of Commerce case could not have set aside the ruling in the Connell Bros. case because the issues involved in the two cases are entirely different. The question at issue in the former case is whether or not the provision of Section 51(e) of the Revenue Code, imposing 5% surcharge and 1% monthly interest on deficiency tax, is mandatory, while the issue in the latter case is whether or not the 25% surcharge imposed by Section 183(a) of the same Code due to failure to pay the percentage tax on any business could be dispensed with where there is no intent to violate the law.

As correctly pointed out by petitioner, the Connell Bros. case squarely supports its position. In both cases, the taxpayers relied upon the ruling of respondent that the mere notation of the phrase "tax included" in the invoice is sufficient compliance of General Circulars Nos. 431 and 440 requiring the separate billing of the sales tax before it can be deducted from the gross selling price for purposes of computing the sales tax due thereon. Since there is admittedly no intentional violation of the law but a mistaken understanding of the regulations laid down by respondent himself, petitioner should not be required to pay the 25% surcharge on the deficiency sales tax.

> We are convinced that appellant, in preparing its sales invoices as it did, was not guilty of an intentional violation of the law. It did not delay filing the returns for the sales taxes corresponding to the period in question, let alone did so purposely. The delay was in the payment of the deficiency, which arose from a mistaken understanding of the regulations laid down by appellee. The ensuing controversy was, in our opinion, generated in good faith and should furnish no justification for the imposition of a penalty. (Connell Bros. [Phil.] v. Coll. of Int. Rev., 9 SCRA 735, 740.)

Petitioner assails the following next three items on the ground that the right of the Government to assess them had already prescribed under Section 331 of the Revenue Code.

1. <u>Billing of Advance Sales Tax, P2,397.17</u> - This amount represents deficiency sales tax and 25% surcharge resulting from the disallowance of the deduction from the gross selling price of advance sales tax billed as a separate item in the invoice covering the months of June, July and

October, 1958, computed as follows:

Advance sales tax billed to customers	₱ 3,835.46
50% sales tax due thereon	₱ 1,917.73
Add: 25% surcharge	479.44
Total Amount due	₱ 2,397.17

2. <u>Tax Exempt Raw Materials, ₱19,915.63</u> -

This represents deficiency sales tax and 25% surcharge arising from the disallowance of the cost of batteries which was deducted from the gross selling price for the period from January 1, 1956 to June 21, 1957, computed as follows:

Cost of batteries used . . .	₱ 31,865.00
50% sales tax due thereon. .	₱ 15,932.50
Add: 25% surcharge	3,983.13
Total Amount due	₱ 19,915.63

The disallowance was based on the ground that locally manufactured batteries were purchased from tax-exempt industries.

3. <u>Deficiency Advance Sales Tax, ₱1,255.42</u> -

This involves deficiency advance sales tax on importations of spare parts in 1958 on the ground that certain incidental expenses and other import charges were not included in determining the advance sales tax, computed as follows:

Total additional importation charges	₱ 14,347.64
Add: 25% Mark-up	3,586.91
Total taxable amount	₱ 17,934.55
7% advance sales tax due . .	₱ 1,255.42

It can be gathered from respondent's memorandum that he is not disputing the fact that the above items pertain to importation and sales in the years 1957 and 1958, which were assessed by respondent only on February 11, 1964 after the lapse of more than 5 years from the filing of the corresponding returns. Respondent, however, contends that the 5-year prescriptive period within which to assess the deficiency taxes had been suspended from March 22, 1960, when petitioner protested the proposed assessment, to February 11, 1964, when the assessment was issued. Respondent further alleges that a reinvestigation was conducted due to the said protest which caused the delay in the issuance of a final assessment. In support of this theory, respondent cited the cases of Republic v. Acebedo, 22 SCRA 1356 and Republic v. Aquias, 33 SCRA 607, wherein it was held that -

> . . . There are cases however where a taxpayer may be prevented from setting up the defense of prescription even if he has not previously waived it in writing as when by his <u>repeated requests or positive acts the Government has been</u>, for good reasons, <u>persuaded to postpone collection</u> to make him feel that the demand was not unreasonable or that no harassment or injustice is meant by the Government. (Underscoring supplied.)

Obviously, the afore-quoted ruling has no application to the case at bar. Petitioner did not make repeated requests or took positive acts which persuaded respondent to postpone the deficiency tax assessment. The records of this case show that there was no request for reinvestigation or "repeated requests" for such reinvestigation. All that petitioner did was to protest the proposed assessment which resulted in its reduction by more than ₱500,000.00.

Moreover, the proposed assessment issued by respondent dated March 14, 1960 is not the tax assessment referred to and contemplated in Section 331 of the Revenue Code, the pertinent portion of which states:

> SECTION 331. Period of limitation upon assessment and collection. - Except as provided in the succeeding section, internal revenue taxes shall be assessed within five years after the return was filed, and no proceeding in court without assessment for the collection of such taxes shall be begun after expiration of such period. . . (Underscoring supplied.)

The tax assessment mentioned therein means an outright or final internal-revenue tax assessment and not a proposed tax assessment. (Brixton Invest. Corp. v. Tabios, CTA Case No. 1681, April 18, 1967.) Also, there is no showing that respondent was prohibited by law, court, or agreement from making the deficiency tax assessment within the prescriptive period which would justify the suspension thereof. In a case of similar import, we held:

> We cannot subscribe to the theory of respondent. In the first place, no provisions of law, orders of the court, or binding agreements were cited by respondent to show that he was prohibited from making the deficiency tax assessment in 1959 or sometime thereafter. In the second place, respondent issued in 1959 a proposed (tentative) deficiency tax assessment against petitioner instead of a formal (final) deficiency tax assessment which he could do to avoid prescription of assessment. Finally, the voluntary and unilateral act of respondent in inviting petitioner to air its objections to the proposed deficiency tax assessment cannot, by any stretch of the imagination, be considered beneficial to respondent in that it suspended the statute of limitations on tax assessment. (Dupro Philippines, Inc. v. Comm. of Int. Rev., CTA Case No. 1341, Dec. 16, 1968; underlining supplied.)

Accordingly, we hold that the right of the Government to assess the three items above-mentioned has already prescribed.

Respondent calls our attention to the fact that in petitioner's letter of March 22, 1960, questioning the proposed assessment it requested that the consideration of the validity of billing sales taxes to its customers by merely noting in its sales invoices the phrase "tax included," be held in abeyance until a final decision is rendered by the Supreme Court in a case still pending in said Court. Assuming arguendo that this is equivalent to a waiver provided in paragraph (b) of Section 332 of the Revenue Code, the same affects only the first item of the assessment, that is, the sum of ₱1,254.69 labeled "Billing of Sales Tax as a separate item" which is conceded by the petitioner not to have prescribed yet. A perusal of said letter will readily show that said request referred to only this item of the proposed assessment and not to the others.

<u>Deficiency sales tax based on sales of Northern Motors, Inc. to customers, ₱734,159.86</u> -

Respondent concedes that the contract of distributorship between petitioner and Northern Motors, Inc. is not one of agency. Stated differently the transactions between the two companies are of purchase and sale. Respondent however urges that the sale by petitioner to Northern Motors, Inc. is a simulated one contrived to evade the payment of the proper tax, Northern Motors being an alter ego of petitioner. In support of this thesis, respondent points to the following circumstances: the finding of the BIR examiner that the prices given to Northern Motors, Inc. were "fantastically low," and that Northern Motors, Inc. was the sole distributor of Rizal Motors, Inc.

If any general rule can be laid down under existing authorities, it is that a corporation will be looked upon as a legal entity until sufficient reason to the contrary appears; but when the notion of legal entity is used to defeat public convenience, justify wrong, protect fraud, or defend crime, the law will regard the corporation as an association of persons; the Court may look beyond the mere artificial personality which incorporation confers (Koppel /Phil.7 Inc. v. Yatco, 77 Phil. 496). Applying these principles to taxation, our Supreme Court held in Yutivo Sons Hardware Co. v. Court of Tax Appeals, 1 SCRA 160; Koppel (Phil.) Inc. v. Yatco, supra; Liddell & Co., Inc. v. Collector of Internal Revenue, G.R. No. L-9687, June 30, 1961, that when one corporation is so organized and controlled and its affairs are so conducted as to make it a branch or agency or dummy of another corporation, or is unreal, or a sham and serves no business purpose and is intended only as a blind, then the corporation may be considered as a mere alter ego of another for tax purposes. Fundamentally, the underlying principle of the doctrine is that transactions between corporations that do not have adverse economic interests do not vary control or change the flow of economic benefit. Hence, to determine whether a corporation is an alter ego of another for tax purposes it is necessary to look at the stockholders behind the corporate structure of the two corporations (Higgins v. Smith, 84 L Ed. 406; Campana Corporation v. Harrison, 114 F. 2d. 400).

Respondent has not presented any evidence whatsoever as to who are the incorporators and stockholders of Rizal Motors and Northern Motors. Indeed, respondent's lone witness Perfecto Valenzuela, BIR examiner, who conducted the investigation that led to the assessment in question, admits that he did not take the trouble of verifying who are the incorporators and stockholders of the two corporations; that the assessment is solely based on the "fantastically low" selling price of Rizal Motors and the fact that Northern Motors was the sole distributor of Rizal Motors; that he, however, admits that he does not know the terms of the contract of distributorship between petitioner and Northern Motors; that he never examined the books of the two corporations; that he does not know the cost of the cars to Rizal Motors after assembly;

that he gathered the selling price of Northern Motors only from some of its customers and used the average for computing the tax liability, but he cannot remember who these customers were; and, to cap it all, that he has no evidence to support his inquiries.

While respondent has not supplied any data as to stockholders of Rizal Motors and Northern Motors, there is, on the other hand, evidence to the effect that the two corporations have adverse economic interest. In petitioner's letter of June 30, 1964, to respondent, petitioner gave a list of incorporators and shareholders of the two corporations, to wit:

	No. of Shares
Incorporators of Rizal Motors, Inc.	
1. Pedro M. SyQuia	249
2. Gonzalo M. SyQuia	248
3. Caridad Cruz de SyQuia	1
4. Ramona Vargas de SyQuia	1
5. Kenneth E. Staley	1
	500
Stockholders of Rizal Motors, Inc. as of December 31, 1963	
1. Pedro M. SyQuia	4,995
2. Caridad Cruz de SyQuia	4,990
3. Fe Cruz Gonzales	5
4. Antonio Avecilla	5
5. Lourdes Alunan	5
	10,000

No. of Shares

Incorporators of Northern Motors, Inc.

1. Yu Khe Thai
2. Yu Eng Poh
3. Yu Khe Siong
4. Yu Khe Jin
5. Alexander SyCip

The correctness of this list has never been controverted by respondent.

The gist of the testimony of Valenzuela recited above, which testimony is the only evidence in support of the assessment in question, clearly shows how superficial was the investigation conducted by the witness, how puerile is his testimony as support for the thesis that Northern Motors is an alter ego of petitioner for tax purposes, and how flimsy, not to say unreliable, is the foundation of the assessment in question. We thus reject respondent's claim that Northern Motors is an alter ego of petitioner, as well as the assessment of ₱734,159.86 in connection therewith.

As to the compromise penalty in the total amount of ₱10,000.00, it is now a well-settled doctrine that compromise penalty cannot be imposed or collected without the aggrement and conformity of the taxpayer (Collector of Internal Revenue v. University of Santo Tomas, et al., G.R. Nos. L-12250 and L-12259, May 27, 1959; The Philippines International Fair, Inc. v. Collector of Internal Revenue, G.R. Nos. L-12928 & L-12932, March 31, 1962).

WHEREFORE, the decision appealed from is hereby reversed, except with respect to the sum of ₱1,003.75, representing deficiency sales tax in 1959 resulting from the failure of petitioner to itemize the sales tax in a sales invoice, which petitioner is hereby ordered to pay within thirty (30) days from the date this decision becomes final.

SO ORDERED.

Quezon City, December 27, 1972.

RAMON L. AVANCEÑA
Associate Judge

WE CONCUR:

ROMAN M. UMALI
Presiding Judge

ESTANISLAO R. ALVAREZ
Associate Judge