REPUBLIC OF THE PHILIPPINES
Court of Tax Appeals
QUEZON CITY

THIRD DIVISION

BPI-PHILAM LIFE ASSURANCE CORPORATION (formerly AYALA LIFE ASSURANCE, INC.),
Petitioner,

-versus-

COMMISSIONER OF INTERNAL REVENUE
Respondent.

CTA CASE NO. 8240
Re: Assessment

Members:

Bautista, Chairperson,
Fabon-Victorino, and
Ringpis-Liban *JJ.*

Promulgated:

MAY 14 2014
9:20 a.m.

x - x

DECISION

RINGPIS-LIBAN, J.:

This is a Petition for Review[1] seeking for the cancellation of Assessment No. VT-2006-000-298[2] for deficiency value-added tax ("VAT") and deficiency premium tax assessments[3] for the taxable year 2006 on the ground of lack of legal and factual foundations.

THE FACTS

Petitioner BPI-PHILAM Life Assurance Corporation (formerly Ayala Life Assurance, Inc.) is a corporation duly organized and existing under and by virtue of Philippine laws and with principal place of business at 15th Floor Ayala-Life-FGU Center 6811 Ayala Avenue, Makati City[4].

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[1] Petition for Review dated March 23, 2011, pursuant to Section 4(a) of Rule 8 of the Revised Rules of the Court of Tax Appeals, in relation to Rule 4 hereof; Docket, pp. 1 to 10, with attachments.
[2] Final Letter of Demand dated December 28, 2009, deficiency VAT of P3,491,801.03, Docket, pp. 820-823, inclusive of details of discrepancies, Exhibit *"B"*.
[3] Final Decision on Disputed Assessment dated January 5, 2011, a deficiency premium tax of P13,201,179.71; Docket, pp. 52 to 57, *Exhibit "H"*.
[4] Joint Stipulation of Facts and Issues dated September 20, 2011; Docket, p. 143.

Petitioner is engaged to carry on the business of insurance and its intermediary services, including but not limited to lending money to its clients or customers without engaging in financing business as contemplated by Republic Act No. 5890[5].

Respondent is the Commissioner of Internal Revenue who is duly appointed and empowered to perform the duties of her office, including among others, the power to decide on administrative protests which have been elevated to her Office in accordance with the provisions of Revenue Regulation No. 12-99, and with office at the Bureau of Internal Revenue ("BIR") National Office Building, Diliman, Quezon City, where she may be served with summons and other court processes[6].

On January 7, 2010, petitioner received a Formal Letter of Demand[7] ("FLD") from respondent dated December 28, 2009 for deficiency income tax amounting to P14,213,413.19[8] and deficiency VAT and amounting to P45,074,711.08[9], inclusive of penalty interests computed up to January 31, 2010, as follows:

Deficiency Income Tax

Gross Profit *per return*		P 114,279,255.00
Add: Disallowed Direct Cost items pursuant to RMC No. 59-2008		
Other Manpower Cost	P 7,849,915.17	
Anticipated Endowments	39,111,189.96	
Taxes and Licenses	82,808,508.57	
Dividends and Premium Credits	68,683,676.41	
Surrenders	108,058,512.08	306,511,802.19
Gross Profit *per audit*		420,791,057,19
Minimum Corporate Income Tax (MCIT) *per audit*		8,415,821.14
Less: MCIT *per return*		2,285,585.10
Discrepancy / Income Tax deficiency		6,130,236.04
Add: Unsupported claims of creditable income tax withheld at source:		
Creditable income tax withheld at source per return	6,293,250.36	
Amount supported per taxpayer's response letter to Letter Notice No. 116-WE-N-06-00-00019 dated 08-31-07	3,932,501.50	2,990,748.86
Income Tax Deficiency		9120984.90

[5] Amended Articles of Incorporation; Docket, pp. 808 to 819, Exhibit *"A-2"*.
[6] *Ibid.*
[7] Inclusive of the Details of Discrepancies and Audit Result / Assessment Notices; Docket, pp. 820 to 827, *Exhibit "B"*.
[8] Assessment No. 2006-000-191
[9] *Ibid.*

Add: Interest – April 16, 2008 to January 31, 2010		5092428.29
Amount Payable		**P 14,213,413.19**

Deficiency Value-added Tax

Income subject to VAT *per audit*:		
Interest income from loans and receivables		P144,054,623.00
Rental income subject to VAT pursuant to Sec. 108 of the NIRC		50,609.419.00
Proceeds of sale of assets, subject to VAT pursuant to Section 106 of the NIRC:		
Motor Vehicles (FS Note 1)	P 4,388,929.00	
Investment properties (real properties, FS Note 12)	48.783.102.00	
Assets held for sale (FS Note 13)	22,946,762.00	76,1,18,793.00
Miscellaneous Income		11,782,601.41
Total		282,565,436.41
Less: Amount subjected per returns		45,726,342.59
Amount not subjected to VAT		236,839,093.82
Output Tax due thereon / Tax deficiency		28,025,959.44
Add: Interest – 1/26/07 to 10/18/10 (0.60832)		17,048,751.64
Amount payable		**P 45,074,711.08**
Over-all tax deficiencies and increments		**P 59,288,124.27**

On February 3, 2010, petitioner filed its Protest[10] against the assessments. Subsequently, on March 30, 2010, petitioner filed additional supporting documents in accordance with Section 228[11] of the Tax Code, as amended.

During a series of discussions with representatives from the BIR Large Taxpayer's Service Division, petitioner conceded that the following items were subject to deficiency income tax and deficiency VAT, respectively:

A. Income Tax

[10] Protest; Docket, pp. 828 to 834, *Exhibit "C"*.

[11] SEC. 228. *Protesting of Assessment*. – When the Commissioner or his duly authorized representative finds that proper taxes should be assessed, he shall first notify the taxpayer of his findings: xxx xxx xxx
The taxpayer shall be informed in writing of the law and facts on which the assessment is made; otherwise, the assessment shall be void.
Within a period to be prescribed by implementing rules and regulations, the taxpayer shall be required to respond to said notice. If the taxpayer fails to respond, the Commissioner or his duly authorized representatives shall issue an assessment based on his findings.
Such assessment may be protested administratively by filing a request for reconsideration or reinvestigation within thirty (30) days from receipt of the assessment in such form and manner as may be prescribed by implementing rules and regulations. Within sixty (60) days from filing of the protest, all relevant supporting documents shall have been submitted; otherwise, the assessment shall become final.
If the protest is denied in whole or in part, or is not acted upon within one hundred eighty (180) days from submission of documents, the taxpayer adversely affected by the decision or inaction may appeal to the Court of Tax Appeals within thirty (30) days from receipt of the said decision, or from the lapse of the one hundred eighty (180) day period; otherwise, the decision shall become final, executor and demandable.

	1.	Direct cost items that may not be claimed:		
		1.1 A portion of "Other Manpower Cost"	P	2,015,221.78
		1.2 Taxes and Licenses	P	82,808,508.57
		1.3 Dividends and Premium Credits	P	68,683,676.41
	2.	Unsubstantiated Creditable Tax	P	2,774,112.09
B.		Value-added Tax ("VAT")		
	1.	Gross Receipts which were not subject to VAT		
		1.1 Proceeds from sale of Motor Vehicle	P	4,388,929.00
		1.2 Proceeds from sale of Real Properties used in business	P	48,783,102.00
		1.3 Miscellaneous Income from scrap sales	P	189,190.42

In a letter[12] dated October 14, 2010, petitioner formalized its offer to settle the conceded revenue and expense accounts. Accordingly, petitioner paid on October 18, 2010 the amount of P9,973,230.08[13] as full settlement of the deficiency income tax assessment and the amount of P11,304,371.62[14] as partial settlement of the deficiency VAT assessment.

Nevertheless, petitioner consistently maintained its position that VAT liability should not be imposed on the interest income on policy loans and all revenue items aggregated under miscellaneous income with the exception of scrap sales which was already conceded.

On February 24, 2011, petitioner received the Final Decision on Disputed Assessment ("FDDA") from respondent with deficiency VAT liability amounting to P3,491,801.03 computed as follows:

Deficiency Value-added Tax

Income subject to VAT *per audit*:		
Interest income from loans and receivables		P 144,054,623.00
Rental income subject to VAT		50,609.419.00
Proceeds of sale of assets, subject to VAT:		
Motor Vehicles	P 4,388,929.00	
Investment properties (real properties)	48.783.102.00	
Assets held for sale (ROPOA)	22,946,762.00	76,1,18,793.00
Miscellaneous Income		11,782,601.41
Total income subject to VAT *per audit*		282,565,436.41
Less: Reinvestigation adjustments – income subsequently verified as not subject to VAT		
Interest Income from Loans and Receivables	144,054,623.00	

[12] Docket, pp. 836 to 838, *Exhibit "E"*.
[13] BIR Form No. 0605 and eFPS payment details dated October 18, 2010; Docket, pp. 341 to 342, *Exhibits "G" and "G-2"*.
[14] BIR Form No. 0605 and eFPS payment details dated October 18, 2010; Docket, pp. 839 to 840, *Exhibits "F" and "F-2"*.

Assets held for sale (ROPOA)	22,946,762.00	167,001,385.00
Income subject to VAT *per investigation*		115,564,051.41
Less: Amount subject to VAT *per returns*		45,726,342.59
Amount not subject to VAT		69,837,708.82
Output Tax due thereon / Tax deficiency (12%)		8,380,525.06
Add: Interest – 1/26/07 to 10/18/10		6,249,805.26
Amount payable *per investigation*		14,630,330.32
Less: Payment made on October 18, 2010		11,304,371.62
Amount still due		3,325,958.70
Add: Interest – 10/19/10 to 01/19/11		165,642.32
Amount payable		**P 3,491,801.03**

Apparently, the FDDA issued by respondent cancelled the original VAT assessment on the proceeds on assets held for sale (ROPOA) amounting to P22,946,762.00 and on interest income on policy loans amounting to P114,054,623.00.

Even so, in addition to the deficiency VAT assessment, the FDDA imposed a five percent (5%) deficiency premium tax on the cancelled interest income on policy loans in the amount of P13,201,179.71, inclusive of penalty interest computed as follows:

Deficiency Premium Tax

Interest Income from Loans and Receivables	P 144,054,623.00
5% Premium Tax due thereon	7,202,731.15
Add: Interest – 01/26/07 to 10/18/10	5,371,461.42
Amount payable per investigation	12,564,192.57
Less: Payment made on October 18, 2010	-
Amount still due	12,564,192.57
Add: Interest – 10/19/10 to 01/18/11	626,987.14
Amount payable	**P 13,201,179.71**

On March 23, 2011, petitioner filed the instant Petition for Review.

In her Answer, respondent averred the following special and affirmative defenses, as follows:

> "8. Petitioner BPI-PHILAM Life Assurance Corporation, is liable to pay its VAT assessment amounting to P3,491,801.03 and deficiency Premium Tax in the amount of P13,201,179.71 in the aggregate amount of P16,692,980.73 for the taxable year 2006 including penalties, surcharges and interest for the following reasons:
>
> 8.1 The instant petition should not be given due course by this Honorable Court for lack of merit.

> 8.2 Respondent respectfully avers that the VAT and Premium Tax Assessments for taxable year 2006 in the aggregate amount of P16,692,980.73 were issued in accordance with the law and regulations.
>
> 8.3 Comprehensive study of petitioner's books of accounts and pertinent accounting records disclosed that it is liable to pay the total deficiency Income Tax, VAT and Premium Tax assessments. xxx xxx xxx."

On September 20, 2011, the parties submitted their Joint Stipulation of Facts and Issues[15] presenting the issues of the case, enumerated as follows:

I. Whether or not petitioner is liable for deficiency VAT in the amount of P3,491,801.03 and deficiency Premium Tax in the amount of P13,201,179.71;

II. Whether or not the interest income on policy loans is subject to the five percent (5%) Premium Tax; and

III. Whether or not respondent's right to issue a deficiency VAT and Premium Tax assessment for the taxable year 2006 is already barred by prescription.

Thereafter, pre-trial was terminated and trial ensued.

On June 10, 2013, petitioner filed its Memorandum. On June 20, 2013, respondent filed her Manifestation that she is adopting the arguments raised in her Answer as her Memorandum. Thereafter this case was submitted for decision.

THE COURT'S RULING

On prescription of respondent's right to issue an assessment

Respondent argued that the deficiency VAT and deficiency Premium Tax assessments were issued in accordance with law and regulations.

On the other hand, petitioner argued that the statute of limitations has set-in and respondent's right to assess and collect internal revenue taxes against petitioner has already prescribed.

We find the petition partly meritorious.

[15] Joint Stipulation of Facts and Issues; Docket, pp. 143-148

Section 203 of the National Internal Revenue Code of 1997, as amended ("Tax Code"), limits the period for respondent to issue an assessment within a period of three (3) years, to *wit*:

> "**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 filing of the return, and no proceeding without assessment for 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." *(Underscoring ours)*

As mandated in the afore-quoted section of the Tax Code, respondent has three (3) years from the last day of the period fixed by law for the filing of the tax return or the actual date of filing, whichever comes later, to assess all internal revenue taxes.

In determining the last day for respondent to assess petitioner for alleged deficiency VAT and premium tax, this Court shall take into consideration the relevant provisions of Section 114 (A) of the Tax Code and Section 2 of Revenue Regulation ("RR") 4-2002 (amending Section 128[16] (A) (1) of the Tax Code), to wit:

> "**Sec. 114.** *Return and Payment of Value-added tax.* –
>
> (A) *In General.* – Every person liable to pay the value-added tax imposed under this Title shall file a quarterly return of the amount of his gross sales or receipts within twenty five (25) days following the close of the taxable quarter prescribed for each taxpayer: Provided, however, that VAT-registered persons shall pay the value-added tax on a monthly basis. *(Underscoring ours)*
>
> "**SEC. 2.** *Time of Filing of Monthly Percentage Tax Return.* – The monthly Percentage Tax Return (BIR Form No. 2551M) of taxpayers, whether large or non-large, shall be filed, and taxes paid, not later than the 20th day following the end of each month, *provided however*, That with respect to taxpayers enrolled with the electronic filing and payment system (EFPS), the deadline for e-Filing the Monthly Percentage Tax Return and e-paying the tax due thereon shall be five (5) days later than the deadline set herein, *provided further*, That for percentage tax returns/other returns required to be filed under Section 120, 125, 126 and 127 of the Tax Code, the shall be filed within the periods stated in those sections." *(Underscoring ours)*

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[16] **Sec. 128.** *Returns and Payment of Percentage Taxes.* –
(A) Returns of Gross Sales, Receipts or Earnings and Payment of Tax. –
(1) Persons Liable to Pay Percentage Taxes. – Every person liable to the percentage taxes imposed under this Title shall file a quarterly return in the amount of his gross sales, receipts and earnings and pay the tax due thereon within twenty-five (25) days after the end of each taxable quarter: Provided, That in case of a person whose VAT registration is cancelled and who becomes liable to the tax imposed in Section 116 of this Code, the tax shall accrue from the date of the cancellation and shall be paid in accordance with the provisions of this Section. *(Underscoring ours)*

The three-year limitation under Section 203 in relation to the afore-quoted statutory provisions is the crux of safeguarding the interests of herein petitioner from the alleged unfounded investigation. In *Commissioner of Internal Revenue vs. FMF Development Corporation*[17], the Supreme Court held that:

> "Under Section 203 of the NIRC, internal revenue taxes must be assessed within three years counted from the period fixed by law for the filing of the tax return or the actual date of filing, whichever is later. This mandate governs the question of prescription of the government's right to assess internal revenue taxes primarily to safeguard the interests of taxpayers from unreasonable investigation. Accordingly, the government must assess internal revenue taxes on time so as not to extend indefinitely the period of assessment and deprive the taxpayer of the assurance that will no longer be subjected to further investigation for taxes after the expiration of reasonable period of time." *(Underscoring ours)*

Based on the dates for filing of petitioner's VAT and percentage tax returns for the taxable year 2006, this Court has determined the period wherein respondent may validly issue an assessment against petitioner, as follows:

Deficiency Value-added Tax

Period Covered	Date of Filing	Last Day to File Return	Last Day to Issue Assessment
1st Quarter	April 24, 2006[18]	April 25, 2006	April 25, 2009
2nd Quarter	July 25, 2006[19]	July 25, 2006	July 25, 2009
3rd Quarter	October 23, 2006[20]	October 25, 2006	October 25, 2009
4th Quarter	January 25, 2007[21]	January 25, 2007	January 25, 2010

Deficiency Premium Tax

Period Covered	Date of Filing	Last Day to File Return	Last Day to Issue Assessment
January	February 23, 2006[22]	February 25, 2006	February 25, 2009
February	March 23, 2006[23]	March 25, 2006	March 25, 2009
March	April 24, 2006[24]	April 25, 2006	April 25, 2009
April	May 23, 2006[25]	May 25, 2006	May 25, 2009
May	June 22, 2006[26]	June 25, 2006	June 25, 2009

[17] G.R. No. 167765, June 30, 2008.
[18] e-filed per Reference No. 100600001029545; Docket, p. 854, Exhibit *"L"*
[19] e-filed per Reference No. 616675319; Docket, p. 858, Exhibit *"M"*
[20] e-filed per Reference No. 100600001291250; Docket, p. 860, Exhibit *"N"*
[21] e-filed per Reference No. 10070000143631; Docket, p. 863, Exhibit *"O-2"*

[22] e-filed per Reference No. 150600000930921; Docket, p. 865, Exhibit *"P-2"*
[23] e-filed per Reference No. 150600000969345, Docket, p. 867, Exhibit *"Q-2"*
[24] e-filed per Reference No. 1506000001027912, Docket, p. 869, Exhibit *"R-2"*
[25] e-filed per Reference No. 1506000001077033, Docket, p. 871, Exhibit *"S-2"*

June	July 21, 2006[27]	July 25, 2006	July 25, 2009
July	August 23, 2006[28]	August 25, 2006	August 25, 2009
August	September 21, 2006[29]	September 25, 2006	September 25, 2009
September	October 20, 2006[30]	October 25, 2006	October 25, 2009
October	November 23, 2006[31]	November 25, 2006	November 25, 2009
November	December 21, 2006[32]	December 25, 2006	December 25, 2009
December	January 25, 2007[33]	January 25, 2007	January 25, 2010

As determined from the foregoing results, respondent had until April 25, July 25, October 25, all in 2009 and January 25, 2010 to assess petitioner for deficiency VAT covering the first, second, third, and fourth quarters of the taxable year 2006.

Whereas, respondent had until February 25, March 25, April 25, May 25, June 25, August 25, September 25, October 25, November 25, December 25, all in 2009 and January 25, 2010 to issue an assessment as to the deficiency Premium Tax.

An assessment is deemed made when notice to this effect is released, mailed or sent to the taxpayer[34]. Due process requires at the very least that such notice must be served on and received by the taxpayer to enable him to determine his remedies thereon[35]. Consequently, an assessment that has not been received by the person liable for the payment of the tax cannot become final and executory[36]. In the instant petition, respondent's FLD dated December 28, 2009 was received by petitioner on January 7, 2010. Consequently, the assessment for deficiency tax made for the first, second and third quarters are well beyond the three-year prescriptive period. Therefore, respondent's assessment is made effective against the petitioner only as to the fourth quarter of the taxable year 2006.

On the other hand, the assessment for deficiency Premium Tax was made known to petitioner for the first time when respondent issued her FDDA dated January 5, 2011. The FDDA, citing RMC No. 49-2010 as basis, thus stated:

[26] e-filed per Reference No. 1506000001124230; Docket, p. 873, Exhibit *"T-2"*

[27] e-filed per Reference No. 1506000001161651, Docket, p. 857, Exhibit *"U-2"*
[28] e-filed per Reference No. 1506000001207406, Docket, p. 877, Exhibit *"V-2"*
[29] e-filed per Reference No. 150600000125806, Docket, p. 879, Exhibit *"W-2"*
[30] e-filed per Reference No. 1506000001289023, Docket, p. 881, Exhibit *"X-2"*
[31] e-filed per Reference No. 1506000001336107, Docket, p. 883, Exhibit *"Y-2"*
[32] e-filed per Reference No. 1506000001378907; Docket, p. 885, Exhibit *"Z-2"*
[33] e-filed per Reference No. 150600000143517; Docket, p. 887, Exhibit *"AA-2"*
[34] First Sumiden Realty, Inc. vs. Commissioner of Internal Revenue, CTA Case No. 8151, September 27, 2012; Commissioner of Internal Revenue vs. United Parcel Service Co., CTA EB Case No. 721 (CTA Case No. 7667), May 16, 2012.
[35] Commissioner of Internal Revenue vs. PASCOR Realty and Development Corporation, G.R. No. 128315, June 29, 1999.
[36] Republic vs. De La Rama, 18 SCRA 861, cited in Estate of the Late Juliana Diez Vda. De Gabriel vs. Commissioner of Internal Revenue, G.R. No. 155541, January 27, 2004.

> "In the light of the recent clarification made under Revenue Memorandum Circular No. 49-2010 that income which are incidental to or in connection with the insurance policy contracts issued are considered akin to premiums and thus subject to the five percent (5%) premium tax instead of VAT, and in view of your clarification that such grant of policy loan is an activity incidental to the insurance business as it is an intrinsic part of the policyholders' respective covenants with you under their insurance policies, we have decided that the said interest income is subject to the 5% premium tax rather than the VAT as we have previously concluded. Thus, we still maintain that the income is subject to business tax, but it is the 5% Premium Tax instead of VAT."

Petitioner argued that the constitutional guarantee of a taxpayer's right to due process was not observed when respondent arbitrarily changed the nature of the deficiency assessment on interest income on policy loans from deficiency VAT to deficiency premium tax in the FDDA.

We find merit in petitioner's argument.

The Supreme Court consistently held that rulings, circulars, rules and regulations promulgated by the Commissioner of Internal Revenue would have no retroactive application if to so apply them would be prejudicial to the taxpayers pursuant to Section 246 of the Tax Code of 1997, which provides:

> "SEC. 246. Non-retroactivity of ruling - Any revocation, modification or reversal of any of the rules and regulations promulgated by the Commissioner shall not be given retroactive application if the revocation, modification or reversal will be prejudicial to the taxpayers, xxx xxx xxx"

Also, this Court finds the provision on non-retroactivity of ruling consistent with the BIR issuance recognized and implemented by respondent in Revenue Memorandum Circular ("RMC") No. 20-1986. The said rule provides for the applicability of Revenue Regulations, Revenue Audit Memorandum Orders, Revenue Circulars and Revenue Memorandum Orders bearing on internal revenue tax rules and regulations, which shall begin to be operative only after due notice thereof may be fairly presumed.

In *Fluor Daniel, Inc. Philippines vs. Commissioner of Internal Revenue*[37], a similar case involving different internal revenue taxes, where respondent changed the category of the assessed deficiency tax upon issuance of the FDDA, this Court held that:

> "xxx xxx xxx We note that, changing the assessment from EWT to FWT only in the issuance of the FDDA would certainly deprive petitioner of the reasonable opportunity to be heard and submit evidence in support of its

[37] CTA Case No. 7793, April 17, 2012

defense, which is a clear violation of due process requirements pursuant to the mandatory provisions of Section 228 xxx xxx xxx"

Hence, respondent's right to issue an assessment against petitioner for the taxable year 2006 has long prescribed when respondent issued the FDDA on February 24, 2011 cancelling the original deficiency VAT assessment on interest income on policy loans and in its stead imposed deficiency Premium Tax for the first time without prior notice and opportunity to protest the same.

Verily, the three (3)-year period mandated by the statute of limitations for issuing an assessment against petitioner has already cut into respondent's right to issue deficiency Premium Tax assessment and deficiency VAT assessment covering the first, second and third quarter, all in the taxable year 2006.

Petitioner is liable for deficiency Value-added Tax

Having determined the veracity of respondent's right to issue an assessment, this Court finds petitioner liable for deficiency VAT but only for the period covering the fourth quarter of the taxable year 2006.

Pursuant to the FDDA issued by respondent, petitioner failed to subject to VAT certain revenue items, as follows: *(a)* rental income in the amount of P50,609,419.00; *(b)* Proceeds from sale of motor vehicles in the amount of P4,388,929.00; *(c)* Proceeds from sale of real property used in business in the amount of P48,783,102.00; and *(d)* certain items of Miscellaneous income in the amount of P11,782,601.41.

Rental Income

Respondent alleged that petitioner failed to report for VAT purposes rental income resulting into an understatement amounting to P4,883,076.41[38]. The amount represents the alleged discrepancy between rental income of P50,609,419.00 as reported in petitioner's 2006 audited financial statements ("AFS") and total income subject to VAT amounting to P45,726,342.59[39] as per petitioner's VAT returns, summarized as follows:

Quarter	Per AFS	Per Return
1st	P 12,537,656.00	P 86,92,114.00
2nd	13,067,231.00	10,769,098.42
3rd	13,930,946.00	12,499,323.50
4th	11,073,585.00	13,765,806.67
Total	P 50,609,419.00	P 45,726,342.59

[38] Answer, Docket p. 80
[39] BIR Docket, p. 161

In its preliminary report dated April 23, 2012, the commissioned Independent Certified Public Accountant ("ICPA")[40] reconciled the above stated difference, quoted as follows:

> **"3. Reconciliation of Vatable Rental Income per Audited Financial Statements (AFS) and per Audit**
>
> We have compared the rental income amount reported in the AFS with the rental income reported in the quarterly VAT returns and we have noted that the AFS amount which is the basis of the BIR's computation of gross receipts subject to VAT used the total amount of rental income which did not include the beginning and ending balances of the accrued rental. Thus, we re-computed the alleged under-declared rental income presented below:

Rental Income per AFS	Php 50,609,419.00
Revenue per VAT returns	45,726,342.59
Difference	4,883,076.41
Less: Increase in accrued income	354,920.41
Unaccounted Difference	Php 4,528,156.00

> <u>The said difference is still subject to further verification as the Company still has to provide us with the documents that would show the details of the aforementioned difference</u>." *(Underscoring ours)*

However, nothing in the supplemental and final report of the ICPA dated August 17, 2012 reverted to verifying the afore-quoted figures and instead limited the discussion within the confines of prescription of respondent's right to issue an assessment. Hence, the amount of P4,883,076.41, inclusive of the increase in accrued rental income, remains unaccounted for.

Well settled is the rule that tax assessments are entitled to the presumption of correctness and made in good faith and it is the duty of the taxpayer to prove otherwise. In case of disputed assessments, the burden of proof is on the taxpayer to establish the fact that it is indeed not liable for any deficiency taxes subject of the assessment. Failure to show documents that would substantiate a claim that no deficiency taxes are due, would result to upholding the validity of the assessment for deficiency [value-added] taxes[41].

Petitioner having failed to substantiate the discrepancy and dispute respondent's claim, all presumptions are in favor of the correctness of respondent's deficiency VAT assessment pertaining to petitioner's rental income, but limited only as to rental income of the 4th quarter in the amount of P11,073,585.00.

[40] Atty. Fredieric B. Landicho, CPA, Tax Partner, Manabat Delgado Amper & Co., member firm of Deloitte Touche Tohmatsu

[41] Camara Steel Industries, Inc. vs. Commissioner of Internal Revenue, CTA Case No. 5960, February 9, 2004.

Also, petitioner argues that out of the total rental income reported in the AFS, the amount of P2,525,694.20 should be excluded as basis for deficiency VAT as it corresponds to rental payments made in 2006 by the Korean Trade Center ("KOTRA"), an alleged VAT-exempt entity.

This Court finds flaw in the petitioner's argument.

Based on records, this court determined that the amount of P1,341,694.20 pertains to rental payments made by KOTRA to petitioner in the 4th quarter of 2006.

In support of its claim that KOTRA is a VAT-exempt entity, petitioner submitted as evidence VAT Exemption Certificate No. 2010-539[42] which provides:

> "This is to certify that the Korea Trade Center (KOTRA) being the trade wing of the Embassy of the Republic of Korea is exempted from value-added tax (VAT) on its official purchases of goods and services in the Philippines based on reciprocity and pursuant to BIR Ruling No. ITAD-037-04 dated April 20, 2004 and Department of Foreign Affairs (DFA) Indorsement dated December 14, 2010." *(Underscoring ours)*

On the face of the document, it is apparent that VAT Exemption Certificate No. 2010-539 was issued on December 28, 2010, long after the year subject of the assessment.

In his cross examination, counsel for respondent pointed out the same as follows:

> "xxx xxx xxx
>
> ATTY. GABRIEL
>
> Q: In Answer to Question No. 11, you mentioned that your basis for stating that Korea Trade Center is VAT-exempt is the VAT Exemption Certificate 2010-539. Am I correct?
>
> MS. GALITA
>
> A: Yes.
>
> ATTY. GABRIEL

[42] See Exhibit I

Q: May I now refer you to the VAT-Exemption Certificate No. 2010-539. It appears Ms. Witness that the date of issuance was December 28, 2010. Am I correct?

MS. GALITA

A: Yes.

ATTY. GABRIEL

Q: Am I also correct to say that the VAT-exemption pertains only to year 2010 onwards or until January 2013?

MS. GALITA

A: Yes.

ATTY. GABRIEL

Q: So, your basis for saying that Korea Trade Center Manila VAT-exempt is this one which bears the date of issuance, December 28, 2010?

MS. GALITA

A: This is the available documents on file with us.

xxx xxx xxx"

Therefore, this Court finds petitioner liable for deficiency VAT on its rental income for the fourth quarter in the amount of P11,073,585.00, undiminished by any exclusion and/or exemption claimed by petitioner.

Gain on Sale of Assets

The presumption of the correctness of the deficiency VAT assessment likewise applies in connection with the proceeds from sale of motor vehicles in the amount of P4,388,929.00 and from sale of real property used in business in the amount of P48,783,102.00.

Records show that for the year 2006, certain dealings in property were reflected in petitioner's AFS consisting of sale of motor vehicles and certain investment properties, as follows:

	Proceeds on Sale	Proceeds on Sale pertaining to 4th Quarter
Motor Vehicle	Php 4,388,929.00	Php 4,388,929.00
Real Properties	48,783,102.00	34,680,101.32

On October 18, 2010, petitioner partially settled the deficiency VAT assessment upon conceding the afore-mention revenue items, including proceeds from sale of scrap aggregated under miscellaneous income.

However, respondent maintained that the assessment on the proceeds from sale of motor vehicles and real properties used in business are unassailable and included the same in the FDDA.

Upon careful scrutiny of the evidentiary documents submitted by petitioner, this Court determined that the deficiency VAT assessment on proceeds of sale of real properties used in business is valid only on dealings made in the 4^{th} quarter of 2006 in the amount of P34,680,101.32.

On the other hand, no evidence in record was found as to which quarterly period the proceeds on sale of motor vehicles are recognized. On petitioner's failure to show that the sale is made on any period other than the 4^{th} quarter of 2006, respondent's assessment for deficiency VAT on proceeds from sale of motor vehicles will not be disturbed.

Miscellaneous Income

Respondent posits that the components[43] of miscellaneous income amounting to P11,782,601.41 are subject to deficiency VAT consequences.

Contrary to respondent's claim, petitioner maintains that, with the exception of the proceeds from scrap sales amounting to P189,190.42 which VAT has already been paid, miscellaneous income are transactions not subject to VAT.

Absent any evidence supporting petitioner's claim that the income items falling under miscellaneous income are transaction not subject to VAT, this Court once again invoke the presumption of correctness of respondent' s deficiency VAT assessment.

In this light, it must be stressed that the burden of proof is on the taxpayer contesting the validity or correctness of an assessment to prove not only that the Commissioner of Internal Revenue is wrong but the taxpayer is right. Otherwise, the presumption of correctness of tax assessments stands[44].

Hence, this Court maintains the presumption of regularity of the assessment made by respondent.

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43 Schedule of Miscellaneous Income for the year-ended December 31, 2006, CTA Docket, p. 964, (Exhibit *'MM'*).
44 Commissioner of Internal Revenue vs. Hantex Trading Co., Inc., G.R. No. 136975, March 31, 2005

Based on the foregoing, this Court rules that petitioner is liable for the following internal revenue tax for the taxable year 2006, computed as follows:

Income subject to VAT:		
Rental income		P 50,609,419.00
Proceeds from sale of assets:		
Motor Vehicles	P 4,388,929.00	
Investment in properties (real properties)	48,783,102.00	53,172,031.00
Miscellaneous income		11,782,601.41
Total		115,564,051.41
Less: Income determined as not subject to VAT		
Rental income for the 1st, 2nd and 3rd Quarter of the taxable year 2006		39,535,833.00
Net income subject to VAT		76,028,218.41
Less: Amount subject to VAT per return – 4th Quarter		13,765,806.67
Amount subject to deficiency VAT		62,262,411.74
Output tax due / deficiency VAT (12%)		7,471,489.41
Add: Penalty interest from January 26, 2007 to October 18, 2010		5,571,888.81
Amount Payable for deficiency VAT, inclusive of interest		13,043,378.22
Less: Payment made on October 18, 2010		11,304,371.62
Amount payable		P 1,739,006.60

Interest Income on policy loans is not subject to premiums tax

In addition to prescription and the non-retroactivity application of BIR issuances, petitioner emphasized that interest income on policy loans is not subject to deficiency premium tax since interest income is not the "premium collected" as provided for in Section 123 of the Tax Code.

Respondent, on the other hand, argued that on the basis of the clarification made under RMC No. 49-2010, income which are incidental to or in connection with the insurance policy contracts issued are considered akin to premiums and thus subject to the five percent (5%) premium tax under Section 123, quoted as follows:

> "With the supporting documents introduced, judicious reexamination of the issues similarly resulted in conclusions favorable to the company and necessitating downward adjustment to the VAT deficiency assessment. This includes adjustment relative to the company's interest income of P144,054,623.00 derived from policy loans granted which was decided upon reinvestigation to be subject to the 5% Premium Tax rather than VAT as per audit. Thus, while there is reduction in the VAT assessment relative to this issue, the reinvestigation finding resulted in deficiency Premium Tax in lieu of the consequent VAT deficiency. The said decision was essentially arrived at in the light of the recent clarification made under Revenue Memorandum Circular No. 49-2010 that incomes which are incidental to or in connection

> with the insurance policy contracts issued are considered akin to premiums and thus subject to the five percent (5%) premium tax instead of VAT, which clarification was taken into consideration together with the company's explanation that such grant of policy loans is an activity incidental to the insurance business as it is an intrinsic part of the policy holders' respective covenants with you under their insurance policies. It is to be noted that this decision is not in agreement with the company's contention that the income is not subject to further business tax as it was derived from investment of the premiums that were already previously subjected to the 5% Premium Tax (or that the said income is neither subject to VAT nor the 5% Premium Tax)."

We agree with petitioner.

The Supreme Court in *Gulf Resorts, Inc. vs. Phil. Charter Insurance*[45], defined an insurance premium as the consideration paid by an insurer for undertaking to indemnify the insured against a specified peril. In Revenue Regulations No. 26[46], premium includes all that is received by the underwriter therefore and is in fact the total consideration receivable for underwriting the risk, whether in one sum or in installments, during the life of the policy.

As provided under Section 123 of the Tax Code of 1997, Premium Tax is imposed on total premiums collected by the life insurance company excluding the premiums collected or received on variable contracts.

In contrast, the term "interest" is defined as income earned from debt claims of any kind. Therefore, interest income earned by petitioner is clearly not a consideration received for underwriting risk but rather income earned from loans and debt instruments of any kind extended to policyholders as mandated under Section 198 of the Insurance Code which provides:

> "SEC. 198. xxx xxx xxx A life insurance company, however, may lend to any of its policyholders upon the security of the value of its policy such sums as may be determined pursuant to the provisions of the policy. xxx xxx xxx."

In justifying the imposition of deficiency premium tax, respondent posited interest income on loans as "akin to premiums" on the basis of RMC 49-2010, thus subject to premiums tax in accordance to Section 123 of the Tax Code, as amended.

The pertinent provision of the circular, is quoted as follows:

> "(2) Management Fees, Rental Income, Commission Income, Re-issuance Fees, Renewal Fees, Other Income/Fees. Management fees, rental income, or any other income earned by the life insurance company from

[45] GR No. 156167, May 16, 2005 citing 43 Am. Jur. 2d 878
[46] DST Regulations dated March 26, 1924

> services which can be pursued independently of the insurance business activity, are thus not subject to the 5% premium tax imposed under Section 123 above but, rather, the same are treated as income from services that are subject to the imposition of VAT pursuant to Section 108 of the Tax Code, as amended, or to the percentage tax imposed under Section 116 of the same Tax Code, as the case may be.
>
> Re-issuance fees, reinstatement fees, renewal fees as well as penalties paid to the life insurance company which are incidental to or in connection with the insurance policy contracts issued are considered akin to premiums, thus, such type of income are covered by Section 123 of the Tax Code and are subject to the five percent (5%) premium tax for the gross amount received on such fees and/or penalties." *(Underscoring ours)*

The afore-quoted circular classified re-issuance fees, reinstatement fees and renewal fees as "akin to premiums," and therefore, subject to premium tax.

We are not impressed.

Under the principle of *ejusdem generis,* interest income may be considered as "akin to premiums" if it is of the same nature as re-issuance, reinstatement and renewal fees which are administrative charges paid in connection with the issuance of policy contracts. This Court is of the opinion that interest income is not an administrative charge related to the issuance of policy contracts but income earned from debt claims, and thus, not "akin to premiums" subject to premiums tax.

Even assuming that RMC No. 49-2010 applies to petitioner's interest income on policy loans for the taxable year 2006, the following provision in the said RMC applies:

> "(3.a.) *Investment Income Realized from the Investment of Premiums Earned.* – Investment income earned by the life insurance companies from investing the premium received in marketable securities, bonds and other financial instruments is considered exempt from the further imposition of business tax since the premiums which have been the source of the funds invested has already been subject to the imposition of the five percent (5%) premium tax imposed by Section 123 of the Code, as amended."

In *Commissioner of Internal Revenue vs. The Philippine American Accident Insurance Company, Inc.*[47], the Supreme Court held that when a company is taxed on its main business, it is no longer taxable further for engaging in an activity or work which is merely part of, incidental to and is necessary to its main business. In the same case, the Supreme Court upheld the rulings of both the Court of Tax Appeals and the Court of Appeals which found that the investment of premiums and other funds received by therein respondents

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[47] GR No. 141658, March 18, 2005.

through the granting of mortgage and other loans was necessary to respondent's business and hence, should not be taxed separately.

WHEREFORE, in the light of the foregoing, the petition is hereby **PARTIALLY GRANTED**.

Assessment No. VT-2006-000-298 against petitioner for deficiency VAT but covering only the first, second and third quarter for the taxable year 2006, and assessment for deficiency premium tax for the same year, is hereby **CANCELLED**. On the other hand, petitioner is held liable for deficiency VAT covering the fourth quarter of the taxable year 2006.

Accordingly, petitioner is **ORDERED** to **PAY** the respondent the amount of **ONE MILLION SEVEN HUNDRED THIRTY NINE THOUSAND SIX AND 60/100 PESOS (P1,739,006.60)** as deficiency VAT.

In addition, petitioner is **ORDERED** to **PAY** deficiency interest at the rate of twenty percent (20%) *per annum* which will be assessed and collected from October 18, 2010 until the full payment of the deficiency VAT.

SO ORDERED.

LOVELL R. BAUTISTA
Associate Justice

ESPERANZA R. FABON-VICTORINO
Associate Justice

Ma. Belen M. Ringpis-Liban

MA. BELEN M. RINGPIS-LIBAN
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 Section 13 of Article VIII 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.

ROMAN G. DEL ROSARIO
Presiding Justice