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REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

PROCTER & GAMBLE PHILIPPINE
MANUFACTURING CORPORATION,
Petitioner,

- versus -

C.T.A. CASE NO. 1897

COMMISSIONER OF INTERNAL
REVENUE,
Respondent.

2/24/82

x - - - - - - - - - - - - - - - x

D E C I S I O N

This is a petition for review of a decision of respondent Commissioner of Internal Revenue dated October 24, 1967 denying the protest of petitioner Procter & Gamble Philippine Manufacturing Corporation (formerly Philippine Manufacturing Company) against an assessment for deficiency sales tax for 1958 in the total amount of ₱160,441.63 consisting of:

Basic deficiency sales tax -	₱120,353.30
25% surcharge - - - - - - - -	30,088.33
Total deficiency tax and surcharge - - - - - - -	₱150,441.63
Compromise penalty - - - - -	10,000.00
Total Amount Due - - - - - - -	₱160,441.63

Petitioner Procter & Gamble Philippine Manufacturing Corporation (formerly Philippine Manufacturing Company) is a corporation duly organized and existing under the laws of the Philippines, with principal office at Sarmiento Building, Ayala Avenue, Makati, Rizal. It is engaged in the manufacture and sale of lard, margarine, soap, cooking oil and other similar coconut oil products.

In a letter dated August 18, 1959 (p. 2, BIR records), respondent informed petitioner that upon investigation conducted by agents of his office, "it was ascertained that as manufacturer you failed to pay the correct sales tax during the year 1958 as a result of the inclusion of the value of materials purchased from contractors in your deductible cost, in violation of sections 183 and 186, penalized under section 209, all of the (then in force) National Internal Revenue Code. There is, therefore, due from you the sum of ₱66,356.63, computed as follows:

Cost of boxes disallowed, represented at 107%	₱811,446.77
Cost of boxes without tax . .	758,361.47
7% tax due on ₱758,361.47 . .	₱53,085.30
25% surcharge thereon . . .	13,271.33
TOTAL AMOUNT DUE & OOLLECTIBLE	₱66,356.63"

A compromise penalty of ₱10,000.00 for extrajudicial settlement of the penal liability for violation of the National Internal Revenue Code was likewise imposed.

A request for reinvestigation was apparently filed by petitioner for under date of September 28, 1962, BIR examiner Jose P. de Castro filed his memorandum on the results of his investigation (Exhs. "1" & "A", pp. 65-67, BIR records), and based on his findings and recommendation a revised assessment was issued on March 12, 1963 by the then Acting Commissioner of Internal Revenue Jose B. Lingad (Exhs. "2" & "A", pp. 73-74, BIR records). To quote:

> Please be informed that upon reinvestigation conducted by an examiner of this Office, it was ascertained that you erroneously deducted from your gross sales of lard, margarine, soap and other similar coconut oil products during 1958, the value of your purchases from contractors as part of your deductible raw materials, in violation of sections 183 and 186, penalized under section 209, all of the National Internal Revenue Code. It was further verified that your claim for tax credit in your monthly returns for November, 1958, was not substantiated as having been allowed by this Office, hence its disallowance. There is, therefore, due from you the sum of ₱150,441.63, computed as follows:
>
> Cost of boxes disallowed,
> represented at 107% - - - ₱811,446.77
> Cost of boxes without tax - ₱758,361.47

7% tax due on ₱758,361.47 - - - -	₱ 53,085.30
Tax Credit disallowed - - - - - -	₱ 67,268.00
Taxes due - - - - - - - - - - - - -	₱120,353.30
25% surcharge thereon - - - - - -	₱ 30,088.33
TOTAL AMOUNT DUE AND COLLECTIBLE	₱150,441.63

> Demand is hereby made upon you to pay the aforesaid sum of ₱150,441.63 within ten (10) days from your receipt hereof.
>
> Should you desire to extrajudicially settle the penal liability arising from your aforesaid violation, you may pay the sum of ₱10,000.00 as compromise penalty in addition to ₱150,441.63, or a total of ₱160,441.63.

In a letter dated May 23, 1963, petitioner protested the afore-quoted assessment. (pp. 133-137, BIR records.) This was followed by another letter-protest dated July 15, 1963. (pp. 129-132, BIR records.)

At this juncture, it may be stated that on May 26, 1964, petitioner, through its treasurer, executed a waiver of the statute of limitation under the National Internal Revenue Code in consideration of the approval by respondent of its request for reinvestigation or reconsideration of the assessment. (p. 141, BIR records). Another waiver of the statute of limitation was executed on December 28, 1966 by petitioner upon request of the then Acting Deputy Commissioner of Internal Revenue. (p. 191, BIR records.)

In a letter dated October 28, 1967, respondent Commissioner of Internal Revenue denied the protests of petitioner dated May 23, 1963 and July 15, 1963. Hence, the instant appeal.

The final decision of respondent denying the protests of petitioner against the assessment for deficiency sales tax and surcharge of ₱150,441.63, aside from the compromise penalty of ₱10,000.00, was arrived at as follows: (Exh. "3", pp. 215-216, BIR records.)

Cost of boxes disallowed represented at 107% - - - - - - -	₱811,446.77
Cost of boxes without tax - - - -	758,361.47
7% tax on ₱758,361.47 - - - - -	₱ 53,085.30
Tax Credit disallowed - - - - - - -	67,268.00
Deficiency sales tax due - - - -	₱120,353.30
25% surcharge thereon - - - - -	30,088.33
TOTAL AMOUNT DUE - - - - - - - -	₱150,441.63

A perusal of the decision appealed from (Exh. "3", pp. 215-216, BIR records; pp. 5-6, CTA records), will readily show that it consists, except the compromise penalty of ₱10,000, of two parts: (1) the 7% sales tax on ₱758,361.47 and (2) the tax credit disallowed in the amount of ₱67,268.00. As explained by respondent in his decision:

> The amount of ₱758,361.47 represents the cost of boxes used as containers of your client's products which was deducted from its gross sales for the period, resulting in the above-mentioned deficiency, Your client claims that it correctly deducted the cost of said boxes because they were purchased from the manufacturers. Investigation, however, reveals that the alleged manufacturers were mere printers which made the boxes in question upon specific orders of your client and which paid only the 3% contractor's tax on their gross receipts. As it was your client that caused the manufacture of said boxes, it is considered the manufacturer thereof, and as the 7% sales tax due thereon had not yet been paid, the cost thereof should not have been deducted from your client's gross receipts.

While the tax credit disallowed in the sum of ₱67,268.00 refers to:

> As regards the amount of ₱67,268.00, which was added to your client's tax liability, our examiner reported that said amount of ₱67,268.00 was deducted by your cleint from its tax liability for the period as alleged tax credit in its favor. However, no such tax credit was authorized by the Commissioner of Internal Revenue in 1958. In other words, without having been granted a tax credit in its favor, your client deducted from the tax due from it alleged overpayment of advance sales tax. We need not stress that under the law, the taxpayer can not <u>motu proprio</u> deduct from its tax liability an alleged tax credit which has not yet been approved.

In his memorandum dated July 29, 1981 filed with this Court, respondent poses two issues before us (pp. 206-207, CTA records):

> (1) Whether or not the cost of containers (boxes and cartons) used by petitioner in the sale of its finished products is deductible from the gross selling price of its finished products such as lard, margarine, soap and cooking oil; and
>
> (2) Whether or not petitioner can automatically deduct from its sales tax liability the amount of ₱67,268.00 representing alleged tax credit which has not been approved or authorized by the Commissioner of Internal Revenue.

The parties are in agreement on the cost of boxes and cartons disallowed and from whom such containers were purchased. As shown in the stipulation of facts filed by them on September 5, 1972 (p. 51, CTA records):

> 1. That cost of containers disallowed (shown gross) were purchased from the following:

a) General Offset Press	₱735,952.74
b) Carmelo & Bauermann	39,258.03
c) Samson Box	36,236.00
Total - 107%	₱811,446.77
Total - 100%	₱758,361.47

Before resolving the question as to whether or not the cost of boxes and cartons used in the sale of petitioner's finished products is deductible from its gross selling price, pertinent to state here is the contention of petitioner that respondent cannot anymore enforce collection of the portion of the assessment under review relating to the disallowance of the cost of boxes and cartons, assuming arguendo that the disallowance of the cost of such containers claimed by petitioner as deductible was proper, on the ground that said assessment had been extinguished by compromise. Considering that a compromise has the effect and authority of res judicata upon the parties (Art. 2037, Civil Code), a finding of the Court that the portion of the assessment relating to the disallowance of cost of containers had been compromised would therefore have the effect of barring respondent from collecting the deficiency sales tax of ₱53,085.30 involved in the assessment.

The records of the case show that petitioner Procter & Gamble Philippine Manufacturing Corporation was assessed by respondent per his letter dated February 14, 1964 deficiency manufacturer's sales tax for the years 1958, 1959, 1960 and 1961 in the sum of ₱1,273,070.41. (Exhs. "B" & "B-1", pp. 69-71, CTA records.) The details of the assessment are as follows: (Ibid)

Taxable amount per investigation (1958-61)			₱57,916,922.55
7% Sales tax due thereon			₱ 4,054,184.58
Less:	Tax withheld by government agency	₱ 942.98	
	Taxes already paid	3,038,785.27	3,039,728.25
Deficiency sales tax due			₱ 1,014,456.33
Add: 25% Surcharge			253,614.08
TOTAL AMOUNT DUE AND DEMANDABLE			₱ 1,268,070.41

And a breakdown of the 1958-1961 deficiency sales tax assessment covers the following periods: (Ibid)

1. Calendar year 1958
2. January to April 1959 and May to December 1959
3. Calendar year 1960
4. Calendar year 1961

The issues appearing in the said 1958-1961 deficiency sales tax assessment are the following: (Ibid)

1. Treatment of sales tax not billed separately to customers as part of taxable sales;

2. Disallowance of certain locally-purchased materials allegedly because the suppliers were subjected to 3% contractor's tax and not to the 7% sales tax;

3. Disallowance of certain imported raw materials on which 7% advance sales tax had been paid on the ground that said materials did not form part of the finished products; and

4. Disallowance of deduction for 2% miller's tax paid on coconut oil milled by our client and used as raw material in the manufacture of lard, margarine and soap.

In its memorandum dated January 28, 1974, contesting the 1958-1961 deficiency sales tax assessment for ₱1,273,070.41 of respondent (Exh. "B", ibid), petitioner clearly and specifically pointed to respondent that a duplication or overlapping assessment exist with respect to the portion corresponding to calendar year 1958 which is covered in this case. To quote the pertinent portion of Exhibit "B" which is marked as Exhibit "B-2" and found on page 78 of the CTA records:

> Under date of October 21, 1967, you issued an assessment against our client based, among others, on the alleged fact that purchases in the amount of ₱758,361.47 were made from

> "contractors" (General Offset Press, Samson Box, and Carmelo & Bauermann). You assessed our client the sum of ₱120,353.30 (excluding 25% surcharge), of which the amount of ₱53,085.30 corresponded to 7% of the disallowance of ₱758,361.47. In addition, you also assessed our client for 25% surcharge amounting to ₱30,088.33, of which the amount of ₱13,271.33 corresponds to surcharge on ₱53,085.30. Said assessment is presently the subject of CTA Case No. 1870 of which your Bureau is or should be aware and should, therefore, take cognizance of. The overlap or duplication consists of the amount of ₱53,085.30 as deficiency 7% sales tax assessment, and 25% surcharge thereon in the amount of ₱13,271.33.

The assessment resulting from the disallowance from the 1958 deductions of petitioner of the cost of cartons and boxes which were purchased from the General Offset Press, Carmelo & Bauermann and Samson Box in the total amount of ₱811,446.77 at 107%, or ₱758,361.47 - 100% (Stipulation of Facts dated August 20, 1972, supra,) appears therefore to be clearly duplicated in the 1958-1961 deficiency sales tax assessment of ₱1,273,070.41 of respondent dated February 14, 1964 insofar as the calendar year 1958 is concerned and respondent's assessment and demand-letter dated October 24, 1967 for the amount of ₱53,085.30

representing 7% deficiency sales tax for 1958 on ₱758,361.47, which is now under review in the present proceeding. The fact of duplicated disallowance of the same items in the 1958-1961 deficiency sales tax assessment and in the case at bar is admitted by respondent. Thus:

"ATTY. MATIC

> Exhibit B-2 is admitted with the following manifestation that the amount of ₱53,085.30 is indeed the subject matter of CTA Case No. 1897 which is the deficiency assessment for sales tax owing to the disallowance of the amount of ₱758,361.47, as deduction claimed by petitioner over the purchases . . .
>
> May I re-phrase my manifestation?
>
> The amount of ₱811,446.77 which represents the cost of boxes disallowed for the period 1958 and that the amount of ₱758,361.47 pertains to the cost of boxes without tax, meaning, which have not been previously taxed at 7%. My admission of Exhibit B-2 is based on this observation, Your Honor."

(t.s.n., September 23, 1977, pp. 26-27)

The records show that by letter dated December 19, 1975, supplemented by letter dated March 20, 1976, petitioner offered to compromise the 1958-1961 deficiency sales tax assessment of

₱1,273,070.41 under Presidential Letter of Instructions No. 208. (See first paragraph, Exh. "C", p. 100, CTA records.) And on June 28, 1976, petitioner received respondent's letter of March 31, 1976 accepting petitioner's offer to compromise the said 1958-1961 deficiency sales tax assessment for the amount of ₱127,307.04 as full and complete settlement of the said assessment. (Exh. "C", ibid.) Said letter reads:

> With reference to your letters of December 19, 1975, and March 30, 1976, I am pleased to inform you that your client's offer to pay ₱127,307.04 payable as follows:
>
> 40% within the month when acceptance of the offer is received, or within five (5) days from such receipt if received at or close to the end of the month;
>
> 20% on or before the 15th of each of the next succeeding 3 months
>
> is hereby accepted pursuant to Letter of Instructions No. 308.
>
> This case will be considered closed and terminated upon presentation of the official receipt covering the payment of the compromise settlement in the amount of ₱127,307.04 as full and complete settlement of the aforementioned assessment to the Chief, Appellate Division, of this Office.

> It would be appreciated if settlement is effected the earliest possible time.

In accordance with the conditions set forth by respondent, petitioner paid the first installment of 40% on July 2, 1976; the second installment of 20% on July 19, 1976; the third installment on August 19, 1976; and the last installment on September 19, 1976. (Exhs. "D", "D-1", "E", "E-1", "F", "F-1", "G" & "G-1", pp. 101-104, CTA records.)

Petitioner Procter & Gamble Philippine Manufacturing Corporation having complied with the conditions imposed by respondent for a full and complete settlement of the 1958-1961 deficiency sales tax assessment, in accordance with respondent's acceptance of compromise, the said 1958-1961 deficiency sales tax assessment may therefore be considered closed and terminated. And since in the deficiency sales tax assessment of ₱120,353.30 now under review, excluding the 25% surcharge, the amount of ₱53,085.30 corresponded to 7% of the disallowance of ₱758,361.47, in addition to the 25% surcharge amounting to ₱30,088.33, of which the sum of ₱13,271.33

corresponds to surcharge on ₱53,085.30, for the year 1958, which is also presently the subject matter of the instant case, is duplicated in the 1958-1961 deficiency sales tax assessment of ₱1,273,070.31, with the compromise settlement of the 1958-1961 assessment under Letter of Instructions No. 308, the portion of the said assessment representing the 7% sales tax on ₱758,301.47, or ₱53,085.30, and surcharge of ₱13,271.33, involved in this case, has been extinguished by compromise settlement. A compromise, being a contract whereby the parties by making reciprocal concessions, avoid a litigation or put an end to one already commenced, has upon the parties the effect and authority of res judicata. (Arts. 2028 & 2037, Civil Code.) A compromise binds the parties even without judicial approval. (Meneses vs. De la Rosa, 77 Phil. 34.) Respondent cannot, therefore, enforce the collection of the ₱53,085.20 as part of the 1958-1961 assessment since it had already been extinguished by compromise.

With this conclusion, it becomes unnecessary to resolve the question posed by respondent whether or not the cost of containers (boxes and cartons) used by petitioner in the sale of its finished products is deductible from the gross selling price of its finished products such as lard, margarine, soap and cooking oil.

Coming to the amount of ₱67,268.00, which was added to petitioner's tax liability, the basis for such an assessment was the absence of legal right to deduct said amount before the refund, or as credit thereof, was approved by respondent Commissioner of Internal Revenue.

The records show that by letter dated August 12, 1958, petitioner filed with the appellate division of the Bureau of Internal Revenue on August 12, 1958 a claim for refund of overpaid advance sales tax collected on its shipments of essential oil. The overpayment was due to BIR Ruling No. 250 dated May 5, 1958 wherein the advance sales tax on essential oil was raised to 50%. After the difference between "essential oils" and "essences" was clarified, the Bureau of Internal Revenue corrected its error by issuing BIR Ruling No. 339, dated June 24, 1958, wherein the advance sales tax on essential oil was again fixed at 7%. (Exhibit "J", p. 110, CTA records.) The claim for refund involves the amount of ₱61,382.00, computed as follows:

Amount paid at 50%:		
(1)	₱11,636.00	
(2)	55,632.00	₱67,268.00
Amount due at 7%:		
(1)	₱ 1,018.00	
(2)	4,868.00	5,886.00
Overpayment:		
(1)	₱10,618.00	
(2)	50,764.00	₱61,382.00

/(1) Entry No. 039152
ex "Pres. Jefferson"
(2) Entry No. 42503
ex "Pioneer Mart."/

(Exhibit "J").

It appears that by letter dated December 9, 1960, petitioner informed respondent that it is withdrawing its request for the refund of the aforesaid amount of ₱61,382.00 as advance sales tax erroneously collected on its shipments of essential oils since it intended to apply this amount to its future sales tax liabilities. This was reiterated in petitioner's letter of December 19, 1960, advising respondent that "Since this action has been taken by our Company, we have no objection if you will consider this matter of the request for refund as closed." (Exh. "L", p. 113, CTA records.) The request was granted by respondent on January 6, 1961 (Exh. "M", p. 112, CTA records) when he informed petitioner that:

> This is to acknowledge receipt of your letter dated December 19, 1960 requesting for the withdrawal of your claim for refund of the total amount of ₱61,382.00 as advance sales tax alleged to have been erroneously paid on your importation of essential oils and to inform you that your said request is hereby granted and the case filed and considered closed.

After petitioner had withdrawn its claim for refund and respondent had granted the same, petitioner, without filing a written claim for tax credit with the Bureau of Internal Revenue, and of course, without authorization by respondent, motu proprio deducted the amount of ₱67,268.00 as tax credit from its sales tax liability for November, 1958. (p. 23, BIR records.) The question now before us is whether petitioner can legally deduct from its tax liability a tax which it claims to have paid erroneously or illegally, without a written claim for tax credit filed with the Commissioner of Internal Revenue within two years after the payment of such tax and without authorization or approval by the Commissioner.

The controlling statute is Section 309 of the then applicable National Internal Revenue Code which authorizes the Commissioner of Internal Revenue to credit or refund taxes erroneously or illegally received, or penalties imposed without authority. The authority of the Commissioner of Internal Revenue to credit or refund taxes or penalties "can only be exercised if the claim for credit or refund is made in writing and filed with him within two years after the payment of the tax or penalty". (Ibid.)

It is quite apparent under the law then applicable that the authority to credit or refund taxes erroneously or illegally received or collected is vested exclusively in the <u>Commissioner of Internal Revenue himself</u>. The law employs the term "<u>Commissioner of Internal Revenue</u>" - without more. Nothing there stated speaks of a taxpayer being authorized unilaterally to deduct from or credit against his tax liability taxes erroneously or illegally paid by or collected from him. Even more, the law imposes the condition that the claim for tax credit or refund must be in writing and filed with the Commissioner of Internal Revenue within two years after the payment of the tax. Where the law authorizes solely the Commissioner of the Internal Revenue to refund or credit taxes erroneously or illegally paid or collected, that authority should not be read to authorize taxpayers to deduct as tax credit from their tax liabilities taxes alleged to have been erroneously or illegally paid by or collected from them without authority from the Commissioner of Internal Reenue, and only after compliance with the requirements imposed by the law.

The law is specific and mandatory. There is no room for interpretation. It merely calls for applications as worded. The purpose is obviously to assure that no tax credit or refund is made without prior investigation or verification by the Commissioner of Internal Revenue to insure that the taxpayer is legally entitled thereto, tax credits or refunds of taxes collected being susceptible easily to abuse to the prejudice of the Government. Public policy would seem to require therefore that no room be left for the exercise of purely personal discretion on the part of taxpayers in the matter of deducting from or crediting against their tax liabilities taxes alleged to have been erroneously or illegally paid by them without prior authority or approval by the Commissioner of Internal Revenue.

On the assumption, therefore, that petitioner has made an overpayment of its advance sales tax liability for the year 1958 in the amount of ₱61,382.00 petitioner cannot *motu proprio* credit such amount against its tax liability without authorization from the Commissioner of Internal Revenue and upon written claim for the tax credit filed with him within two years from collection of the tax. Accordingly, petitioner Procter & Gamble Philippine Manufacturing Corporation is hereby ordered to pay to respondent Commissioner of Internal Revenue the amount of ₱84,085.00 representing deficiency sales tax due for 1958 and 25% surcharge thereon, computed as follows:

Tax credit disallowed . . .	₱67,268.00
25% surcharge thereon . . .	16,817.00
Total amount due	₱84,085.00

Although the claim for tax refund was only for ₱61,382.00, the amount petitioner actually deducted from or credited against its November 1958 sales tax liability was ₱67,268.00. (p. 23, BIR records.)

WHEREFORE, the decision appealed from is hereby modified in the sense that respondent cannot anymore enforce collection of the deficiency sales tax of ₱53,085.30 and affirmed insofar as it disallows the tax credit of ₱67,268.00. With costs against petitioner.

SO ORDERED.

Quezon City, Metro Manila, February 26, 1982.

AMANTE FILLER
Presiding Judge

WE CONCUR:

CONSTANTE C. ROAQUIN
Associate Judge

ALEX Z. REYES
Associate Judge