REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

FIRST DIVISION
****

SKY INTERNET, INCORPORATED,
Petitioner,

C.T.A. CASE NO. 6587

Members:

- versus -

ACOSTA, *Chairman*
BAUTISTA, and
CASANOVA, *JJ.*

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:

AUG 10 2005

x - x

DECISION

BAUTISTA, L., J.:

This case seeks for the cancellation of Assessment Notice with Demand No. 43453 dated April 30, 2002 issued by respondent assessing petitioner of deficiency income taxes in the total amount of **TWO MILLION FORTY FIVE THOUSAND EIGHT HUNDRED NINETY FIVE AND 18/100 PESOS (P2,045,895.18)** covering the taxable year 1998.

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

Petitioner is a corporation duly organized and existing under Philippine laws, with principal office address at 4th Floor, Bayantel Building, 234 Roosevelt Avenue, San Francisco Del Monte, Quezon City, Metro Manila *(par 1.1, Joint Stipulation of Facts and Issues)*. Under its Amended Articles of Incorporation, petitioner is engaged in the business of providing, selling, and supporting communication and information product and network services to individual consumers, corporations, government agencies and other organizations *(par 1.2,* *Joint Stipulation of Facts and Issues).*

As of May 22, 1998, petitioner has the following stockholders with Sky Vision Corporation (Sky Vision) owning 99.84% of petitioner's outstanding capital stock, to wit:

Stockholders	No. of Shares Subscribed	Percentage
Sky Vision	2,496	99.84%
Eugenio Lopez III	1	0.04%
Carlos V. Tria, Jr.	1	0.04%
Carlo Katigbak	1	0.04%
Enrique Olives	1	0.04%
TOTAL	2,500	100.00%

As per the petitioner's General Information Sheet dated May 12, 1998 submitted to the Securities and Exchange Commission, Sky Vision is a domestic corporation duly organized and existing under Philippine laws. It is authorized to operate as a consulting firm in the field of marketing and programming through the rendering of professional services and expertise in cable television; distribute cable hardwares and programs; and engage in the construction of cable and MATV and other related systems *(pars. 1.3-1.5 , Joint Stipulations of Facts and Issues).*

During the calendar year 1997, petitioner secured cash advances or loans from Sky Vision in the aggregate amount of Twenty One Million Pesos (P21,000,000.00) which it used as working capital for its current operations *(par 1.7, Joint Stipulation of Facts and Issues).*

For the calendar year 1998, petitioner incurred interest expenses on the said cash advances from Sky Vision in the amount of Three Million Seven Hundred Eighty One Thousand Eight Hundred Thirteen and 60/100 Pesos (P3,781,813.60) which it deducted from its gross income for purposes of computing its taxable income for taxable year 1998 *(pars. 1.8-1.9, Joint Stipulation of Facts and Issues).*

On April 30, 1999, petitioner filed its Annual Income Tax Return for the calendar year 1998 and reported therein a net loss of One Hundred Sixty Eight Thousand Five Hundred Twenty Three Pesos (P168,523.00) *(par. 1.10, Joint Stipulation of Facts and Issues).*

On May 20, 2002, petitioner received respondent's Formal Letter of Demand and Assessment Notice No. 43453 dated April 30, 2002 assessing it of deficiency income taxes including interests in the aggregate amount of Two Million Forty Five Thousand Eight Hundred Ninety Five and 18/100 Pesos (P2,045,895.18) covering the calendar year 1998. The Details of Discrepancies as attached contained the following:

> "Disallowed Interest Expense – Investigation revealed that the interest expense claimed in the amount of P3,872,767.82 can not be allowed as expense due to the following reasons:
>
> 1. P3,781,813.60 – this was paid to Sky Vision, a wholly-owned subsidiary of Sky Internet, hence said expense is unallowable pursuant to Section 34 (B)(2)(b) in relation to Section 36 of the National Internal Revenue Code of 1997.
>
> 2. P 90,954.22 – this amount was not deducted against interest income subjected to Final Withholding Tax, thus, disallowed."

Consequently, a Request for Reconsideration thereof was filed by the petitioner on June 19, 2002. Without receiving any response from the respondent within the period allowed by law, petitioner deemed it proper to elevate this instant petition on January 15, 2003 for the consideration of this Court.

On March 11, 2003, respondent filed his Answer, raising the following as his Special and Affirmative Defenses:

> 7. The investigation conducted by the respondent's examiners reveal *(sic)* that the Interest Expense claimed in the amount of P3,872,767.82 cannot be allowed as deductible expense from income earned for the following reasons:
>
>   7.1 interests in the amount of P3,781,813.60 was paid to Sky Vision, a wholly owned subsidiary of petitioner, hence said expense is unallowable pursuant to Section 34 (B)(2)(b) in relation to Section 36 of the National Internal Revenue Code of 1997, thus disallowed;
>
>   7.2 interests in the amount of P90,954.22 was not deducted against interest income subject to Final Withholding Tax, thus disallowed;
>
> 8. The assessment for deficiency income tax in the amount of P2,045,895.18 is valid and in accordance with law;

9. Assessments are prima facie presumed correct and made in good faith;

10. The burden of proof is upon the petitioner to prove that the assessment issued by the respondent is indeed null and void;

11. All assessments and pre-assessment notices were issued and sent to the

12. petitioner in accordance with well-established procedures.

Upon the filing of petitioner's Memorandum dated April 14, 2005, this case was deemed submitted for decision on April 21, 2005 sans the memorandum of respondent.

The issues as stipulated by the parties are as follows:

1. Whether or not respondent erred in disallowing the deduction from petitioner's gross income of the interest petitioner paid to Sky Vision in the aggregate amount of Three Million Seven Hundred Eighty One Thousand Eight Hundred Thirteen and 60/100 Pesos (P3,781,813.60) based on Section 34(B)(2)(b) in relation to Section 36 of the 1997 Tax Code;

2. Whether or not respondent erred in disallowing the deduction of interest income (should be "expense") in the amount of Ninety Thousand Nine Hundred Fifty Four and 22/100 Pesos (P90,954.22); and

3. Whether or not the Request for Reconsideration was filed within the thirty (30) day period.

Although the issue on prescription is not among the issues stipulated above, petitioner raised the same in its memorandum alleging that the assessment notice dated April 30, 2002 issued by the respondent was already barred by prescription considering the petitioner filed its income tax return for the taxable year 1998 on April 30, 1999 and three years therefrom is until April 29, 2002 only and not April 30, 2002. Thus, this Court deems it necessary to discuss first the issue of whether or not the Formal Letter of Demand and Assessment Notice No. 43453 were issued within the reglementary period allowed by law, pursuant to Section 203 of the 1997 National Internal Revenue Code, which provides that:

> **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. *(Emphasis supplied)*

Noteworthy is the fact that the issuance of an assessment is vital in determining the period of limitation regarding its proper issuance and the period within which to protest it. Section 203 of the 1997 National Internal Revenue Code mandates that internal revenue taxes must be assessed within three years from the last day prescribed by law within which to file the necessary return. Necessarily, the taxpayer must be certain that a specific document constituting an assessment must have been issued and well within the prescriptive period, else, confusion as to the period to issue an assessment and make a corresponding protest would arise. An assessment is relevant in the proper pursuit of judicial and extra judicial remedies to enforce the taxpayer's liabilities and certain matters that relate to it, such as the imposition of surcharges and interest, and in the application of statutes of limitations and in the establishment of tax liens *(Vitug and Acosta, Tax Law and Jurisprudence, 1st Edition [1997], p. 267).*

In the instant case, petitioner filed its Annual Income Tax Return for the taxable year 1998 on April 30, 1998. Pursuant to Section 203 of the 1997 NIRC, where a return was filed beyond the last day prescribed by law for the filing of the return, respondent has the period of three (3) years from the day the return was actually filed, within which to issue his assessment for petitioner's deficiency tax liabilities. At the outset, it would seem that respondent, when he issued and released the Formal Letter of Demand and Assessment Notice No. 43453 on April 30, 2002, had timely and validly issued the subject assessment. In accordance with Article 13 of the Civil Code of the Philippines, when the law speaks of years, it shall be understood that years are of 365 days each. Consequently, the three (3)-year prescriptive period for assessment under Section 203 of the 1997 NIRC has an aggregate number of 1095 days (365 days x 3 years), reckoned from the date prescribed by law for the filing of the return or from the actual filing of said return, whatever the case may be. In other words, the three (3)-year prescriptive period expires on the 1095th day notwithstanding the fact that within that period, there is a leap year which consists of 366 days in a year.

In the case at bar, when the questioned assessment notice was issued and released on April 30, 2002, a total of 1096 days have already lapsed since there are 29 days in the month of February 2000, being a leap year. Accordingly, a careful analysis of the facts and circumstances surrounding the case would reveal that respondent only had until April 29, 2002 within which to issue the assessment. The undisputed issuance and release of the subject assessment notice on April 30, 2002, is clearly issued one day after the expiration of the period of limitation.

It must be stressed that internal revenue taxes are self-assessing and no further assessment by the government is required to create the tax liability *(Tupaz vs. Ulep, G.R. No. 127777, October 1, 1999)*, thus, the reason for the imposition of the prescriptive periods or the statute of limitations for the issuance of assessments. The prescriptive period allows the government to act properly and promptly in making the assessments, and on the other hand, gives the taxpayers the feeling of security against unscrupulous tax agents who would find an excuse to inspect the books of taxpayers, not to determine the latter's real liability but to take advantage of every opportunity to molest law-abiding citizens. If courts can be very strict in not allowing the taxpayers to avail of its right to claim for refunds filed beyond the prescriptive period of two (2) years, the more courts are particular and firm in not allowing invalidly issued assessments to affect the rights of the taxpayers against its effects.

Moreso, the running of the three (3)-year period allowed by law is subject to some exceptions and one of which is found under Section 222(b) of the 1997 NIRC, which provides that:

> Section 222. *Exceptions as to the Period of Limitation of Assessment and Collection of Taxes. –*
>
> (a) xxx
>
> (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.

Based on the above provision of law, the three (3)-year period to assess is extended by the valid execution of a waiver to be executed by the parties. In this case, there was no valid waiver executed, hence, the subject Formal Letter of Demand and Assessment Notice issued against petitioner are void for having been issued beyond the 3-year prescriptive period. Consequently, the government's right to issue an assessment for the said period has already prescribed.

But even assuming, for the sake of argument, that the subject assessment notice was issued within the prescriptive period allowed by law, a close scrutiny of the records of the case nevertheless shows that petitioner is not liable for the deficiency tax assessed against it.

Respondent, in his Assessment Notice, disallowed some expenses of petitioner assigning the same as discrepancies, to wit:

> a. P3,781,813.60 – this interest expense was paid to Sky Vision, a wholly-owned subsidiary of Sky Internet hence said expense if unallowable pursuant to Section 34 (B)(2)(b) in relation to Section 36 of the National Internal Revenue Code of 1997; and
>
> b. P 90,954.22 – this interest expense was not deducted against interest income subjected to Final Withholding Tax, thus disallowed.

Petitioner, on the other hand, argues that the said interest expenses it had incurred were ordinary and necessary business expenses as they represent interest on indebtedness incurred in the pursuit of its communication and information product and network service business. Thus, the said interest expenses are deductible from gross income pursuant to Section 34 (B)(3) of the 1997 National Internal Revenue Code. Furthermore, petitioner avers that respondent erred in considering that petitioner and Sky Vision as related parties defined under Section 36 (B)(3) of the same Code considering that no stockholder owns directly or indirectly more than fifty (50) percent of the outstanding stock of each corporation.

This Court finds petitioner's arguments impressed with merit.

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Sections 34 (B), 34(B)(2)(b) and 36 (B)(3) of the 1997 National Internal Revenue Code (NIRC) specifically provide that:

> **SEC. 34. Deductions from gross income.** – Except for taxpayers earning compensation income arising from personal services rendered under an employer-employee relationship where no deductions shall be allowed under this Section other than under Subsection (M) hereof, in computing taxable income subject to income tax under Sections 24(A); 25(A); 26; 27(A), (B) and (C); and 28(A)(1), there shall be allowed the following deductions from gross income:
>
> xxx xxx xxx
>
> **(B) Interest** –
>
> (1) **In General** - The amount of interest paid or incurred within a taxable year on indebtedness in connection with the taxpayer's profession, trade, or business shall be allowed as deduction from gross income; Provided, however, that the taxpayer's otherwise allowable deduction for interest expense shall be reduced by an amount equal to the following percentages of the interest income subjected to final tax:
>
> **Forty-one percent (41%) beginning January 1, 1998**;
> Thirty-nine percent (39%) beginning January 1, 1999; and
> Thirty-eight percent (38%) beginning January 1, 2000.
>
> (2) **Exceptions** – No deduction shall be allowed in respect of interest under the succeeding subparagraphs:
>
> xxx xxx xxx
>
> (b) If both the taxpayer and the person to whom the payment has been made or is to be made are persons specified under **Section 36 (B)**; or
>
> xxx xxx xxx
>
> **SEC. 36. Items not Deductible** –
> Xxx
>
> (B) Losses from Sales or Exchanges of Property. - In computing net income, no deduction shall in any case be allowed in respect of losses from sales or exchanges of property directly or indirectly –
>
> xxx xxx xxx
>
> (3) Except in cases of distributions in liquidation, **between two corporations more than fifty percent (50%) in value of the outstanding stock of each of which is owned, directly or indirectly, by or for the same individual**, if either one of such corporations, with respect to the taxable year of the corporation preceding the date of the sale or exchange was, under the law applicable to such taxable year, a personal holding company or a foreign personal holding company.
> *(Emphasis supplied)*

Based on the foregoing provisions of law, interest expenses are allowed as a deduction from gross income but subject to certain exceptions as provided for under Section 34(B)(2) of the 1997 NIRC. It is specifically provided under the said section that if both the taxpayer and the person to whom the payment has been made or is to be made are persons specified under Section 36(B), then the interest expense incurred or shall be incurred shall not be allowed as a deduction from the gross income.

In order then for interest expense to be deductible, it must be shown that there is an indebtedness, that the same is that incurred by the petitioner, and that there must be a legal liability to pay interest.

In this instant case, it is not disputed that the loans or indebtedness from where the subject interest expenses arose were incurred by petitioner. Inasmuch as compliance with the first two requisites is not disputed *(par. 1.7, Joint Stipulation of Facts and Issues)*, this Court will now discuss the third requisite. To do so, it is important to discuss the relationship between petitioner and Sky Vision, or the party to whom the interest expense had been made in order to determine whether their relationship is covered by the provision on related parties under Section 36(B)(3) of the 1997 NIRC.

Under Section 36(B)(3) above quoted, two corporations will be considered related parties, if they satisfy the following essential requirements:

a) More than 50% in value of the outstanding stock of each is owned directly or indirectly by or for the same individual; and

b) If either one of such corporations is with respect to the taxable year of the corporation preceding the date of the sale or exchange, was, under the law applicable to such taxable year, a personal holding company or a foreign personal holding company.

Based on the evidence on record, petitioner and Sky Vision should not be treated as related parties because no individual owns, directly or indirectly, more than fifty percent (50%) of the outstanding capital stock of petitioner and Sky Vision. As stipulated by the parties, a majority of the outstanding shares of stock of petitioner in 1998 was owned by

Sky Vision *(par. 1.3, Joint Stipulation of Facts and Issues; Exhibit E)*. On the other hand, Sky Vision's shares of stock in 1998 were owned by various stockholders, as follows:

SKY VISION CORPORATION
(as of 12 August 1998)

Stockholder	No. of Shares Subscribed	Percentage
Lopez, Inc.	348,826,990	42.4778229%
Benpres Holdings Corp.	162,463,400	19.7837087%
Buenavista Holdings Corp.	81,231,600	9.8918421%
Legaspi Capital Holdings Corp.	81,231,600	9.6047372%
Pioneer Score Phils., Inc.	78,873,900	0.3998427%
Trans-Service Corp.	3,283,500	0.3998427%
Acris Corp.	5,635,400	0.6862414%
RMJ Devt. Corp.	5,532,200	0.6736744%
FEBTC Group Trust	845,700	0.1029837%
First Phil. Industrial Corp.	625,000	0.0761083%
Midland Pacific Devt.	488,300	0.0594619%
Lakandula Insurance Factors	676,100	0.0823309%
Federico M. Garcia	35,197,300	4.2860923%
Eugenio Lopez III	3,249,300	0.3956781%
Bienvenido Tesoro	2,346,500	0.2857411%
Mel V. Velarde	2,000,000	0.2435467%
Jose Corpus	698,600	0.0850708%
Chicano Devt. Corp.	1,977,900	0.2408555%
Arturo Macapagal	343,300	0.0418048%
Exequiel Magsaysay	477,700	0.0581711%
Robert Coyuito, Jr.	907,700	0.1105336%
Eugenio Lopez, Jr.	1	0.0000001%
Oscar M. Lopez	1	0.0000001%
Manuel M. Lopez	1	0.0000001%
Augusto Almeda Lopez	1	0.0000001%
Rommel S. Duran	1	0.0000001%
Carlos V. Tria, Jr.	1	0.0000001%
Edwin Villanueva	1	0.0000001%
Leo Antonio T. Lagon	1	0.0000001%
Esteban Pacannuayan	1	0.0000001%
Eduardo L. David	1	0.0000001%
Treasury Shares	4,285,900	0.5219083%
Total	**821,197,900**	**100.000%**

(Exhibit H)

However, Lopez, Inc., which owns 42.78% of Sky Vision, is likewise owned by three (3) different corporate entities and four (4) individuals, to wit:

LOPEZ, INC.
(as of 23 July 1998)

Stockholder	No. of Shares Subscribed	Percentage
Crosto Holdings Corporation	20,665	25.831%
Crème Investment Corporation	20,666	25.833%
Presta Holdings Corporation	17,999	22.499%
Eugenio Lopez, Jr.	1	0.001%
Oscar M. Lopez	1	0.001%
Manuel M. Lopez	20,666	25.833%
Presentacion Psinakis	1	0.001%
Eugenio Lopez III	1	0.001%
TOTAL	**80,000**	**100.000%**

(Exhibit N)

Meanwhile, the respective stock ownership of the above corporate stockholders of Lopez, Inc. are as follows:

CRÈME INVESTMENT CORPORATION
(as of 10 March 1998)

Stockholder	No. of Shares Subscribed		Percentage
	(Common)	(Preferred)	
Eugenio Lopez, Jr.	4,809	11,419,852	1.2258%
Conchita Lopez	2,500		0.6372%
Eugenio Lopez III	55,001		14.0195%
Regina Roy	55,001		14.0195%
Rafael Lopez	55,001		14.0195%
Maria Rosario Grassi	55,001		14.0195%
Roberta delos Reyes	55,001		14.0195%
Ernesto Lopez	55,001		14.0195%
Ramon Lopez	55,001		14.0195%
Oscar M. Lopez	1		0.0003%
Manuel M. Lopez	1		0.0003%
Camilo D. Quiason	1		0.0003%
TOTAL	**392,319**	**11,419,852**	**100.00%**

(Exhibit N-1)

CROSLO HOLDINGS CORPORATION
(as of 19 April 1998)

Stockholder	Subscribed	Percentage
Oscar M. Lopez	58,345	52.605%
Consuelo R. Lopez	52,558	47.388%
Paz Mercedes Vargas	1	0.001%
Oscar Martin R. Lopez	1	0.001%
Beatriz Eugenia Puno	1	0.001%
Ma. Presentacion Abello	1	0.001%
Elvira Carmen Abello	1	0.001%
Federico Daniel R. Lopez	1	0.001%
Benjamin Ernesto R. Lopez	1	0.001%
Angela Cristina R. Lopez	1	0.001%
TOTAL	**110,911**	**100.000%**

(Exhibit N-2)

PRESTA INVESTMENT CORPORATION
(as of 19 April 1998)

Stockholder	No. of Shares Subscribed (Common)	No. of Shares Subscribed (Preferred)	Percentage
Presentacion Psinakis	396	18,000	99.00%
Margarita Fragante	1		0.25%
Rommel S. Duran	1		0.25%
Lauro Panganiban III	1		0.25%
Zenaida Tanada	1		0.25%
TOTAL	**400**	**18,000**	**100.00%**

(Exhibit LL)

Based on the foregoing shareholdings, the individual stockholders of Lopez, Inc. and their respective attributed percentage ownership in petitioner and Sky Vision are as follows:

Stockholders	Percentage of Ownership in Lopez, Inc. (By Individuals)	Percentage of Ownership in Sky Vision	Percentage of Ownership in Sky Internet
Manuel M. Lopez	25.83%	16.17%	16.14%
Presentacion L. Psinakis	22.28%	13.94%	13.91%
Oscar M. Lopez	13.59%	8.51%	8.49%
Consuelo R. Lopez	12.24%	7.65%	7.64%
Ernesto Lopez	3.64%	2.28%	2.28%

Eugenio Lopez III	3.65%	2.28%	2.28%
Maria Rosario Grassi	3.64%	2.28%	2.28%
Rafael Lopez	3.64%	2.28%	2.28%
Ramon Lopez	3.64%	2.28%	2.28%
Regina Roy	3.64%	2.28%	2.28%
Roberta delos Reyes	3.64%	2.28%	2.28%
Eugenio Lopez, Jr.	0.33%	0.20%	0.20%
Lauro Panganiban III	0.06%	0.04%	0.03%
Margarita Fragante	0.06%	0.04%	0.03%
Rommel S. Duran	0.06%	0.04%	0.03%
Zenaida Tanada	0.06%	0.04%	0.03%
Conchita Lopez	0.00%	0.00%	0.00%
Angela Cristina R. Lopez	0.00%	0.00%	0.00%
Beatriz Eugenia Puno	0.00%	0.00%	0.00%
Benjamin Ernesto R. Lopez	0.00%	0.00%	0.00%
Camillo D, Quiason	0.00%	0.00%	0.00%
Elvira Carment L. Abello	0.00%	0.00%	0.00%
Federico Daniel R. Lopez	0.00%	0.00%	0.00%
Oscar Martin R. Lopez	0.00%	0.00%	0.00%
Paz Mercedes Vargas	0.00%	0.00%	0.00%
Presentacion Abello	0.00%	0.00%	0.00%
	100.00%	62.59%	62.46%

As clearly shown above, no individual stockholder owns more than 50% of the outstanding capital stock of each of petitioner and Sky Vision. Manuel M. Lopez, Presentacion Psinakis and Oscar M. Lopez, who are brothers and sister, together own only 38.62% of Sky vision and 38.54% of petitioner.

It is clear from the provisions of the law that only those interest expenses incurred between related parties pursuant to Section 36(B) of the 1997 NIRC are not allowed as deductions from gross income. Considering that petitioner and Sky Vision are not related parties as defined under Section 36(B) of the 1997 NIRC, the deduction of the subject interest expenses from petitioner's gross income is proper.

As regards the disallowed interest expense in the amount of P90,954.22, this Court likewise finds the same to be erroneous.

Petitioner maintains that the interest income of P90,954.22 should not be included anymore in the income subject to income tax because the same has already been subjected to final withholding tax. On the other hand, it was alleged by respondent in its Schedule of Discrepancies that the claimed interest expense for 1998 in the amount of P90,954.22 was not deducted against interest income subjected to Final Withholding Tax, thus disallowed *(pp. 519 & 704, BIR Records).*

Both arguments are untenable. Indeed, under Section 34(B)(1) of the 1997 NIRC, the taxpayer's allowable deduction for interest expense for the year 1998 must be reduced by an amount equivalent to forty one percent (41%) of its interest income subject to final tax for the said year. However, a careful scrutiny of petitioner's Income Tax Returns *(pp. 52 & 54, BIR Records)* and General Ledger Abstract *(pp. 361 & 364, BIR Records)* for 1998 shows that petitioner's total interest income subject to final withholding tax is in the amount of P221,839.57. The same documents likewise discloses that the amount of P90,954.22, which was disallowed by respondent as deduction, represents 41% of the interest income of P221,839.57. Consequently, the interest expense of P9,886,030.00 deducted by petitioner from its taxable gross income for the same year was already net of the amount of P90,954.22. Clearly then, it was erroneous on the part of the respondent to disallow the said amount of P90,954.22 since this amount was never claimed as a deduction by the petitioner against its gross income for the taxable year 1998.

IN VIEW OF ALL THE FOREGOING, the subject Petition for Review is hereby **GRANTED.** Accordingly, the Formal Letter of Demand and Assessment Notice No. 43453 assessing petitioner of deficiency income tax liabilities in the amount of **TWO MILLION FORTY FIVE THOUSAND EIGHT HUNDRED NINETY FIVE PESOS AND 18/100 PESOS (P2,045,895.18)** for the taxable year 1998, are hereby **CANCELLED** and **SET ASIDE**.

SO ORDERED.

LOVELL R. BAUTISTA
Associate Justice

WE CONCUR:

ERNESTO D. ACOSTA
Presiding Justice

CAESAR A. CASANOVA
Associate Justice

CERTIFICATION

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

ERNESTO D. ACOSTA
Chairman, First Division
Presiding Justice