REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

EN BANC

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

-versus-

SPLASH CORPORATION,
Respondent.

C.T.A. EB No. 330
(C.T.A. Case No. 7197)

Present:

Acosta, P.J.
Castañeda, Jr.
Bautista,
Uy,
Casanova, and
Palanca-Enriquez, JJ.

Promulgated:
MAY 0 5 2008

x---x

D E C I S I O N

BAUTISTA, J.:

Before Us is a Petition for Review[1] filed by herein petitioner on December 7, 2007, praying for the reversal of:

(1) the Decision dated May 29, 2007 of the Second Division of the Court ("Court in Division") in C.T.A. Case No. 7197,

[1] *Rollo*, pp. 7 - 41, with Annexes.

granting herein respondent's claim for refund in the amount of Forty Seven Million Four Hundred Sixty Nine Thousand Five Hundred Forty Eight and 29/100 Pesos (P47,469,548.29) representing its excess income taxes paid for its exempt products for the taxable year 2002; and

(2) the Resolution dated October 30, 2007 denying herein petitioner's Motion for Reconsideration.

Antecedent Facts

The antecedent facts, as narrated by the Court in Division in its Decision, are as follows:

> "Petitioner[2] is a domestic corporation organized and existing under Philippine laws with office at the HBC Corporate Centre, 2nd Floor, No. 548 Mindanao Avenue, Quezon City. It is engaged primarily to manufacture, bottle, pack, and market cosmetics and other beauty products in the Philippines and overseas. It is large-scale taxpayer duly registered with the Bureau of Internal Revenue with Tax Identification No. 001-096-221-000. It is likewise registered as a withholding agent, and as such, withheld taxes on the wages/salaries of its employees and on income payments to individuals or corporations subject to the expanded withholding tax.
>
> As the inventor/owner of various skin care composition products, petitioner was issued Certificate of Utility Model/Design Registration Numbers UM-8471, 2-1997-15095 and 2-1999-00320 by the Bureau of Patents and the Intellectual Property Office on December 23, 1997, June 29, 2000 and September 19, 2000, respectively, for the registration of its patented products under the brand names Extraderm Plus, Extract and Maxipeel.

[2] Herein Respondent.

On the other hand, respondent Commissioner[3] is the head of the Bureau of Internal Revenue (BIR) with office address at the BIR National Office, Diliman, Quezon City.

For the taxable period 2002, petitioner, on April 14, 2003, paid its annual income taxes in the total amount of Sixty Five Million Five Hundred Ninety Four Thousand Six Hundred Thirty Seven and 76/100 (P65,594,637.76).

On September 28, 2004, in view of petitioner's application for a tax exemption pursuant to the tax incentives as provided for under Republic Act No. (R.A.) 7459, or otherwise known as the Inventors and Inventions Incentives Act of the Philippines, for the following Patent Registration/Utility Model Nos., to wit:

1. UM-8471 – A Skin Care Composition for the Treatment of Acne and Pigmentary Disorder
2. 2-1997-15095 – A Skin Care Composition for Use as a Facial Cleanser
3. 2-1999-00320 – A Skin Care Composition

the BIR Deputy Commissioner for Legal and Inspection Group Jose Mario C. Buñag issued a ruling confirming petitioner's entitlement to the income tax exemption under Section 6 of the said R.A., which exemption could be availed of during the first ten (10) years from the date of the first sale on a commercial scale, subject to specific conditions, registration processes, as well as, payment of taxes not covered by the incentive.

In this regard, petitioner then filed on April 7, 2005 an administrative claim for refund for its alleged excess income taxes paid for the taxable year 2002 in the amount of P47,469,548.29 computed as follows:

Regular Corporation Income Tax (paid on April 14, 2003)	P65,594,637.79
Less: Regular Corporate Income Tax (after taking Into consideration the income Tax exemption granted)	18,125,089.50
Total Refundable	**P47,469,548.29**

[3] Herein Petitioner.

Without waiting for the decision of the respondent and before it would be barred by prescription, petitioner then elevated this appeal to this Court through a Petition for Review on April 12, 2005.

In his Answer filed on June 14, 2005, respondent raised the following as his Special and Affirmative Defenses:

> '4. Petitioner's alleged claim for refund/tax credit is subject to administrative routinary examination/investigation by the respondent's Bureau;
>
> 5. Petitioner failed miserably to show that the total amount of Php 47,469,548.29 claimed as overpaid income tax for taxable year 2002 was erroneously or illegally collected, or that the same was properly documented;
>
> 6. Taxes paid and collected as presumed to have been paid in accordance with law; hence, not refundable;
>
> 7. In an action for tax refund/credit, the taxpayer has the burden to establish its right to refund, and failure to sustain the burden is fatal to the claim for refund;
>
> 8. It is incumbent upon petitioner to show that it has complied with the provisions of Section 204 in relation to Section 229 of the Tax Code; and
>
> 9. Well-established is the rule that refund/tax credits are construed strictly against the taxpayer as they partake the nature of exemption from tax.'

It is noted that, after hearing and presentation of evidence, petitioner, in its Memorandum filed on December 5, 2006, modified its prayer/relief to show the amount of **P52,665,854.33** (instead of the original prayer of P47,469,548.29) representing its overpaid income taxes for the year 2002, which amount is based on the Report of the Court-Commissioned Certified Public Accountant. This case was subsequently submitted for decision on December 18, 2006, sans respondent's Memorandum.

The parties stipulated the following as the issues of the case:

1. Whether or not the respondent Commissioner can disregard the income tax holiday ('ITH') incentives to which the petitioner is entitled under Republic Act

('R.A.') No. 7459, otherwise known as the 'Investors and Inventions Act of the Philippines.'

2. Whether or not the petitioner overpaid its income tax for the year ended December 31, 2002.

3. Whether or not the petitioner is entitled to the claim for refund for the excess income taxes paid for the taxable year 2002. "[4] *(Citations omitted)*

The Ruling of the Court in Division

On May 29, 2007, the Court in Division granted herein respondent's Petition for Review and ordered herein petitioner to refund respondent the amount of P47,469,548.29 representing its excess income taxes paid for its exempt products for the taxable year 2002.

The Court in Division found that respondent had satisfactorily shown that, on separate dates of December 23, 1997, June 29, 2000 and September 19, 2000, it was issued Certificates of Registration for its utility models, UM-8471, 2-1997-15095 and 2-1999-000320, respectively, of skin care compositions by the Bureau of Patent and Intellectual Property Office of the Philippines. For this reason, it is entitled to the income tax exemption under Section 6 of Republic Act No. 7459, otherwise known as "The Inventors and Invention Incentives Act" ("RA 7459"). Under the said law, any income derived by respondent from the sale of its patented products is exempt from the payment of income taxes for a period of ten (10) years from the date of the product's first sale on a commercial scale.

[4] *Rollo*, pp. 22 – 26, Assailed Decision dated May 29, 2007, pp. 1 – 5.

However, as regards the amount of refund respondent is entitled to as a result of its overpayment, the Court in Division ruled that it cannot grant respondent's modified claim as this is more than what is being asked for in the administrative claim for refund, as well as, in the Petition filed before the Court in Division. According to the Court in Division, the difference of P5,196,306.04 (P52,665,854.33 - P47,469,548.29) not included in respondent's claim for refund was already deemed waived.

It thus disposed of the case as follows:

> "WHEREFORE, this instant Petition for Review is **GRANTED.** Accordingly, respondent is hereby **ORDERED** to **REFUND** to petitioner the amount of **FORTY SEVEN MILLION FOUR HUNDRED SIXTY NINE THOUSAND FIVE HUNDRED FORTY EIGHT AND 29/100 PESOS (P47,469,548.29)** representing petitioner's excess income taxes paid for its exempt products for the taxable year 2002.
>
> SO ORDERED."[5]

On June 25, 2007, herein petitioner filed a Motion for Reconsideration[6] of the Decision dated May 29, 2007.

On July 9, 2007, herein respondent filed a Motion to Expunge/Reject (Re: Motion for Reconsideration dated 25 June 2007).[7] In the said Motion, respondent prayed that the Motion for Reconsideration filed by herein petitioner be expunged from the records for the following reasons: (1) the Motion did not indicate the time and date of hearing; (2) the respondent

---

[5] *Rollo*, p. 32, Assailed Decision dated May 29, 2007, p. 11.
[6] *Records*, C.T.A. Case No. 7197, pp. 484 - 492.
[7] *Id.*, pp. 494 – 502.

failed to include the material dates to determine the timeliness of the Motion; (3) the Motion is defective in substance; and (4) the Motion is *pro-forma*.

On September 11, 2007, the Court in Division issued a Resolution denying the Motion to Expunge/Reject for lack of merit.[8]

Subsequently on October 30, 2007, the Court in Division denied herein petitioner's Motion for Reconsideration.[9]

The Issues

Hence, the instant recourse where petitioner raises the following grounds:

> I. The Honorable Court's Second Division erred in holding that income derived by respondent from its sales of its patented products in taxable year 2002 are exempt from payments of income taxes because respondent's exemption covers a period of ten (10) years from the date of the product sale on commercial scale.
>
> II. The Honorable Second Division did not touch upon the implication of Revenue Regulation (RR) No. 19-93 in arriving at a conclusion.
>
> III. The Honorable Second Division erred in entertaining the instant case.

---

[8] *Records*, C.T.A. Case No. 7197, pp. 544 – 546.
[9] *Rollo*, pp. 34 – 38, Assailed Resolution dated October 30, 2007, pp. 1 – 5.

The Ruling of the Court En Banc

The Petition for Review has no merit.

The administrative and judicial claims for refund were filed within the period set by law

We shall first resolve the third ground raised by petitioner.

The fact that the judicial claim for refund was filed by respondent only on April 12, 2005, or barely a few days after it filed its administrative claim for refund on April 7, 2005 does not make the administrative claim *pro forma*.

As explained by respondent in its Comment, it filed the administrative refund only on April 7, 2005 as BIR Ruling DA-506-2004 dated September 24, 2004[10] confirming respondent's eligibility to the tax incentives under RA 7459, came to the knowledge of the respondent at a much later date.

Besides, a taxpayer cannot be faulted for taking advantage of the full two-year period set by law for filing his claim for refund for there is no provision in the Tax Code requiring that the claim for refund be filed at the earliest instance in order to give the Commissioner an opportunity to rule on it and the Court to review the ruling of the Commissioner of Internal Revenue on appeal.

---

[10] *Rollo*, pp. 84 - 86.

Moreover, it bears stressing that when the two-year period is about to prescribe and the claim for refund with the Commissioner of Internal Revenue has not been acted upon, for the protection of the interest of the taxpayer, he should file a petition for review with this Court within the said two-year period; otherwise, if the decision of the Commissioner is adverse to the taxpayer and it was made after the two-year period he can no longer appeal the same to this Court.[11] This is precisely what respondent did and it cannot be faulted for doing so.

Respondent is entitled to its claim for refund

We shall now proceed to the first and second grounds. Being closely interrelated, We shall discuss them jointly.

There is no dispute that respondent, on separate dates of December 23, 1997, June 29, 2000 and September 19, 2000, was issued Certificates of Registration for its utility models, UM-8471, 2-1997-15095 and 2-1999-000320, respectively, of skin care compositions by the Bureau of Patent and the Intellectual Property Office of the Philippines. Neither is there any question that respondent as a registered inventor of these products is entitled to the tax incentives under RA 7459.

---

[11] Commissioner of Internal Revenue v. Hitachi Computed Products (Asia) Corporation, CA-G.R. SP No. 63340, February 7, 2002.

The only issue in this case is the implication of Section 4 (B) of Revenue Regulations No. (R.R.) 19-93[12] on respondent's claim. Petitioner is of the view that since under R.R. 19-93 the effectivity of the tax exemption commences on the date of the approval of the application for tax exemption, in this case on September 28, 2004, the sales of tax exempt designs and products of respondent for the year 2002 are not covered. In short, petitioner contends that only claims for refund subsequent to the issuance of the September 28, 2004 BIR Ruling may be covered by the income tax exemption.

We are not persuaded.

It is well-settled that all administrative issuances must not override, but must remain consistent and in harmony with the law they seek to apply and implement as administrative rules and regulations are intended to carry out, neither to supplant nor modify, the law.[13] In case of discrepancy between the basic law and an implementing rule or regulation, the former prevails.[14]

Section 6 of RA 7459 provides that:

---

[12] "SECTION 4. *Conditions for Availment of Tax Incentives and Tax Exemptions.* —

xxx xxx xxx

B. Upon approval of the application, a Certificate of Tax Exemption shall be issued by the Commissioner of Internal Revenue which shall be effective on the date of approval thereof."

[13] Commissioner of Internal Revenue v. Deutsche Bank AG Manila Branch, C.T.A. EB No. 113 (C.T.A. Case No. 6566), September 19, 2006.

[14] Philippine Petroleum Corporation v. Municipality of Pililla, Rizal, G.R. No. 90776, 198 SCRA 82, June 3, 1991.

"SECTION 6. *Tax Exemption.* — To promote, encourage, develop and accelerate commercialization of technologies developed by local researchers or adapted locally from foreign sources including inventions, any income derived from these technologies **shall be exempted from all kinds of taxes during the first ten (10) years from the date of first sale**, subject to the rules and regulations of the Department of Finance. Provided, that this tax exemption privilege pertaining to invention shall be extended to the legal heir or assignee upon death of the inventor.

The technologies, their manufacture and sale, shall also be exempt from payment of license, permit fees, customs duties and charges on imports." *(Emphasis Ours)*

From the foregoing provision, it is clear that any income derived from respondent's inventions shall be exempted from all kinds of taxes **during the first ten (10) years from the date of first sale.** The reason for this exemption is to encourage Filipino inventors to create more inventions and innovations beneficial to the people and to the country.[15]

Section 2 of RA 7459 reads:

"SECTION 2. *Declaration of National Policy and Program.* — It is hereby declared to be the national policy to give priority to invention and its utilization on the country's productive system and national life; and to this end **provide incentives to inventors** and protect their exclusive right to their invention, **particularly when the invention is beneficial to the people and contributes to national development and progress.**

Pursuant to the national policy, **the Government shall provide a program to set up a climate conducive to invention and innovation, give encouragement and support to inventors** who are creative and resourceful, as well as imbued with a deep sense of nationalism, and **maximize the capability and productivity of inventors though incentives and other forms of assistance and support.**" *(Emphasis Ours)*

Thus, to accept petitioner's view that only claims for refund subsequent to the issuance of the BIR ruling approving the application for income tax exemption should be granted, would not only be inconsistent with under Section 6 of RA 7459 which expressly states that "any income derived from these technologies shall be exempted from all kinds of taxes during the first ten (10) years from the date of first sale," but would also defeat the spirit and intent of the law.

In fact, it is well to note that the subject BIR Ruling itself acknowledges that the said exemption can be availed of during the first ten (10) years from the date of the first sale on commercial scale.

A perusal of the records of the case reveals that respondent was able to show that the income taxes paid by it for its exempt products for the taxable year 2002 are well within the period of ten (10) years from the date of its first sale in commercial scale. Ms. Lilia D.C. Francisco, the Accounting Manager of Splash Corporation from 1999 to 2004, declared in her judicial affidavit[16] that the utility models, UM-8471, 2-1997-15095 and 2-1999-000320, were first sold as patented products in the year 2001, 1997, and 1999, respectively. We find no reason to suspect the veracity of her statement as it is supported by the income tax return ("ITR")[17] and supporting audited financial statements submitted by respondent. In fact,

[16] *Records*, C.T.A. Case No. 7197, pp. 142 – 143, Exhibit "I."
[17] *Id.*, pp. 148 – 149, Exhibit "B."

respondent's testimonial and documentary evidence were never disputed by petitioner. And contrary to the claim of petitioner, respondent complied with all the requirements stated in the BIR Ruling as respondent is duly registered with the BIR as a withholding agent and withholds taxes on the wages/salaries of employees and on income payments to individuals or corporations subject to the expanded withholding tax.[18] Thus, We find no reason to deny respondent's claim for refund.

Considering that respondent paid thru error or mistake and the petitioner accepted the payment, the principle of *solutio indebiti* under Article 2154 of the New Civil Code, which provides that "if something is received when there is no right to demand it, and it was unduly delivered through mistake, the obligation to return it arises," must be applied, as aptly ruled by the Court in Division.[19]

To recover the amount paid thru error or mistake, the following must be established: (1) that there was an actual collection and receipt by the Government of the tax sought to be recovered, and (2) that he has complied with the statutory requirements relative to the two-year prescriptive period for filing claims for refund.[20]

---

[18] *Records*, C.T.A. Case No. 7197. p. 114, Joint Stipulations of Facts, p.1.
[19] *Rollo*, p. 37, Assailed Resolution dated October 30, 2007, p.4.
[20] Feliciano C. Badillo, represented by Rudy C. Badillo v. Commissioner of Internal Revenue, C.T.A. Case No. 5320, June 10, 1998.

In this case, respondent was able to show that it indeed filed and paid its 2002 income taxes. Records also show that the respondent filed its claim for refund within the two-year prescriptive period. Petitioner therefore has the obligation under the law to refund the erroneously paid taxes of respondent.

It has been said that: "A taxpayer should not be held to suffer loss by his good intention to comply with what he believes is his legal obligation, where such obligation does not really exist. When money is paid to another under the influence of a mistake of fact, that is to say, on the mistaken supposition of the existence of a specific fact which would not have been known that the fact was otherwise, it may be recovered. The ground upon which the right of recovery rests is that money paid through misapprehension of facts belongs in equity and in good conscience to the person who paid it."[21]

In closing, We reiterate the ancient principle that no one, not even the State, shall enrich oneself at the expense of another.[22] In the field of taxation where the State exacts strict compliance upon its citizens, the State must likewise deal with taxpayers with fairness and honesty for the harsh power of taxation must be tempered with evenhandedness.[23]

---

[21] Far East Bank and Trust Company v. Commissioner of Internal Revenue, C.T.A. Case No. 6050, August 8, 2001.
[22] Citibank, N.A. v. Court of Appeals, G.R. No. 107434. 280 SCRA 459, October 10, 1997.
[23] Filinvest Development Corporation v. Commissioner of Internal Revenue, G.R. No. 146941, 529 SCRA 605, August 9, 2007.

WHEREFORE, the instant Petition for Review is hereby **DISMISSED.** Accordingly, the Decision dated May 29, 2007 and Resolution dated October 30, 2007 are hereby **AFFIRMED.**

SO ORDERED.

LOVELL R. BAUTISTA
Associate Justice

WE CONCUR:

ERNESTO D. ACOSTA
Presiding Justice

JUANITO C. CASTAÑEDA, JR.
Associate Justice

ERLINDA P. UY
Associate Justice

CAESAR A. CASANOVA
Associate Justice

OLGA PALANCA-ENRIQUEZ
Associate Justice

CERTIFICATION

Pursuant to Section 13, Article VIII of the Constitution, it is hereby certified that the above Decision has been reached in consultation with the members of the Court *En Banc* before the case was assigned to the writer of the opinion of this Court.

ERNESTO D. ACOSTA
Presiding Justice