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REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

PHILIPPINE DAIRY PRODUCTS CORPORATION,
Petitioner,

- versus -

C.T.A. CASE NO. 4824

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:
JUL 10 1996

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DECISION

Case at hand refers to the assessments issued against petitioner Philippine Dairy Products Corporation (PDCP for brevity) involving alleged deficiency sales and expanded withholding taxes, inclusive of increments for the year 1985, in the respective amounts of P23,971,805.41 and P1,466,042.78 or a total sum of P25,437,848.19.

Petitioner is a registered domestic corporation engaged in the production, marketing and distribution of dairy products.

In a letter of demand (p. 7, CTA records) accompanied with assessment notices dated October 28, 1988, respondent demanded from petitioner payment of the total amount of P25,437,848.19, as deficiency sales and expanded withholding taxes for 1985, computed as follows:

1985 - Deficiency Sales Tax

Particulars	Amount	Tax Rate	Tax Share
Sales (subject to 10%)	P 9,068,234.70	10%	P 906,823.47
Sales (subject to 5%)	247,429,324.38	5%	12,371,466.22
Total Basic taxes			13,278,289.69
Less: Tax paid			940,637.13
Deficiency sales tax			P12,337,652.56
Add: 25% surcharge			3,084,413.14
20% interest p.a. up to 10-28-88			8,549,739.71
TOTAL AMOUNT DUE AND COLLECTIBLE			P23,971,805.41

1985 - Deficiency Expanded Withholding Tax

Professional Services rendered by SMC to PDPC	P16,302,987.43
5% Tax due thereon	P 815,149.37
Add: 25% surcharge	203,787.34
20% interest p.a. up to 10-28-88	446,806.07
Compromise penalty	300.00
TOTAL AMOUNT DUE AND COLLECTIBLE	1,466,042.78

The deficiency sales tax assessment was brought about by the disallowance of the total sales tax credits claimed by PDCP in 1985, for alleged failure to comply with the uniform method of accounting for sales tax and sales tax credit prescribed in Revenue Regulations (RR for short) No. 19-84.

The deficiency expanded withholding tax (EWT for brevity) arose out of PDCP's failure to withhold 5% tax on its payments to San Miguel Corporation (SMC for short) for the professional services rendered by the latter to the former.

Not in agreeable with the said assessments, on December 14, 1988, petitioner filed with the B.I.R. its protest letter dated December 13, 1988 (pp. 10-12, CTA records). Contained in its protest was its allegation, that it made substantial compliance with RR No. 19-84. Hence, its claim for sales tax credit for the year 1985 should not be disallowed by the B.I.R.

With regard to its deficiency EWT assessment, petitioner averred in its protest letter, that the alleged professional fees paid to SMC were mere reimbursements, and therefore, not income subject to withholding tax.

On October 30, 1989, petitioner filed with the B.I.R. a supplemental protest (pp. 13-14, CTA records) advancing additional/new defenses against aforesaid assessments. Relative to its deficiency sales tax assessment, petitioner once again assailed RR No. 19-84, but this time on more grounds, to wit:

> 1. It is not valid, for it was not published in the Official Gazette;
>
> 2. It is illegal, for it is contrary or in conflict with E.O. No. 990, the law which it sought to implement; and
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> 3. It is arbitrary, unreasonable, harsh and oppressive, for it disallowed total claims

> for tax credits, simply because PDCP failed to observe literally the accounting system prescribed in the regulations.

Anent its expanded EWT assessments, petitioner asserted in its supplemental protest letter, that the recipient-payee of the alleged professional fees had reported and declared said fees in its income tax return, and the tax due thereon was duly paid to the B.I.R.

Despite petitioner's invocation of additional grounds in its supplemental protest, in a letter dated December 12, 1989 (pp. 15-19, CTA records) respondent still denied petitioner's protest or request for reconsideration.

Petitioner believed that respondent's denial letter, failed to consider the issues raised in its supplemental protest. Hence, on March 16, 1990, it filed with B.I.R. its letter of March 15, 1990 (pp. 21-22, CTA records), requesting for consolidated resolution on various protested assessments, and at the same time a reconsideration of respondent's December 12, 1989 decision, so that the issued raised in the supplementary protest could be passed upon.

Pursuant to petitioner's second request for reconsideration, respondent's Appellate Division conducted an investigation on petitioner's subject assessments. During the investigation, petitioner presented documentary and testimonial evidence to support its position against the assessments. Notwithstanding all the evidence presented by petitioner, respondent was not convinced to reconsider her previous decision. The second request for reconsideration of petitioner was denied again in respondent's letter of May 13, 1992, which was received by the former on June 9, 1992. Hence, on June 25, 1992, petitioner filed the instant appeal with this Court.

Respondent filed his Answer (pp. 53-59, CTA records) on September 15, 1992 alleging several special and affirmative defenses, the most pertinent of which are as follows:

> 1. The deficiency sales tax assessment was based on the disallowance of the total sales tax credits of petitioner for the year 1985, for its failure to comply with the sales tax credit accounting method prescribed under RR No. 19-84, and which requirement is mandatory;
>
> 2. The deficiency assessment on the expanded withholding tax, was based on the failure of petitioner to withhold 5% from payments made to SMC, pursuant to a Joint Venture Agreement entered between petitioner and SMC, for which said payment constitutes service income for SMC;
>
> 3. The assessment has not prescribed upon its issuance on October 28, 1988 for the year 1985, since the percentage tax return is to be filed on or before the twentieth day of the second month following the close of the taxable year (Sec. 193, NIRC, as amended);

4. The assessment was issued in accordance with law; and

5. All presumptions are in favor of the correctness of the tax assessments.

The issues to be resolved in this case are the following:

1. Whether or not the right of respondent to assess the deficiency sales tax has already prescribed;

2. Whether or not RR No. 19-84, the legal basis for the deficiency sales tax assessment, is valid; and

3. Whether or not petitioner is liable to the deficiency expanded withholding tax.

As regards the first issue, petitioner contends that respondent's right to assess the deficiency sales tax for 1985 has already prescribed. On the contrary, respondent avers such right to assess has not prescribed, for Section 193 of the Tax Code provides that percentage tax return is to be filed on or before the twentieth day of the second month following the close of the taxable year (par. 14, p. 6, Answer; p. 58, CTA rec.).

The averment of respondent is untenable. Such provision of Section 193 is no longer found in the 1985 Tax Code, which should be applied as the year involved in the sales tax in question is 1985. The provision cited by respondent is found in the Tax Code of 1984 and prior years, and its pertinent portion is quoted hereunder:

"Sec. 193. *Payment of percentage taxes.*

(a) In general. - (1) Declaration and payment of quarterly gross sales, receipts, etc. - Unless otherwise specifically provided it shall be the duty of every person conducting a business on which a percentage tax is imposed under this Title, to render a quarterly declaration on a cumulative basis of the amount of his, her or its gross sales, receipts or earnings or gross value of output actually removed from the factory or mill warehouse and to compute the tax due thereon.

(i) For each of the first three quarters of the taxable year, the tax so computed shall be decreased by the amount of tax previously paid and by the sum of the tax credits allowed under this title for the preceding and current quarters. The tax due shall be paid not later than twenty days following the close of each of the first three quarters of the taxable year xxx xxx xxx.

(ii) Final Annual Percentage Tax Return. - On or before the twentieth day of the second month following the close of the taxable year, every person liable to tax under this Section shall file a final percentage tax return covering the total gross sales receipts or earnings or gross value of output actually removed from the factory or mill warehouse for the preceding calendar or fiscal year. xxx xxx ." (Underscoring supplied)

As can be gleaned from the above-quoted provisions, the phrases "on a cumulative basis" and "final annual percentage tax return" are expressly used. The express use of such words "cumulative" and "final" signifies the clear intention of the law, to consider the first three (3) quarterly declarations of sales or receipts and the payments of sales taxes due thereon, as mere partial declarations of sales and partial payments of sales tax.

Upon filing of the final annual percentage tax return, the first three quarterly declarations of receipts and sales taxes paid are accumulated or added together, and the final sales tax due is thereafter computed and paid.

Owing to such cumulative treatment of the quarterly percentage sales tax returns, the then prescriptive period of five (5) years to assess, is reckoned from the due date of filing the final annual percentage tax return, following the principle enunciated in the case of **Gibbs vs. Collector of Internal Revenue**, G.R. No. L-13453, February 29, 1960. If only this provision of Section 193 of the 1984 Tax Code, could be made applicable to the case at bar, the respondent's defense against prescription would definitely hold water. Her right to assess the subject 1985 deficiency sales tax, would be deemed as having not prescribed, for the counting of the three (3) year prescriptive period would start from the due date of the filing of the final annual percentage tax return, which was on January 20, 1986. From this date up to October 28, 1988, only 2 years, 9 months and 8 days had lapsed, and therefore, respondent's right to assess the deficiency sales tax had not prescribed. Unfortunately, however, such provision is inapplicable to the subject sales tax assessment.

As rightfully argued by petitioner, it is Section 193 as amended by P.D. 1959, which should properly govern. Section 11 of said decree which became effective January, 1985, states that:

> "Section 11. Section 193 of this Code, as amended, is hereby further amended to read as follows:
>
> 'Section 193. *Payment of percentage taxes.*
>
> (a) In general. - (1) Declaration and payment of quarterly gross sales, receipts, etc. - Unless otherwise specifically provided, it shall be the duty of every person conducting a business on which a percentage tax is imposed under this Title, to render a quarterly declaration of the amount of his, her or its gross sales, receipts or earnings or gross value of output actually removed from the factory or mill warehouse and to compute the tax due thereon.
>
> xxx xxx xxx
>
> The tax due shall be paid not later than twenty days following the close of each quarter. xxx" (Underscoring supplied)

It will be noted from the above-cited provisions, that the word "cumulative" was no longer used to describe the quarterly percentage tax returns to be filed. Petitioner is, therefore, right in claiming that Section 193 (now renumbered as Section 162 of the 1985 Tax Code) no longer requires the filing of cumulative quarterly sales tax. Its theory that percentage sales tax returns are now non-cumulative is strongly supported by Revenue

Memorandum Circular No. 35-84, pertinent portion of which provides:

> "xxx
>
> The non-cumulative quarterly return shall be filed for the fiscal quarters commencing after December 31, 1984, not later than the 20th day after the close of each quarter.

Fiscal Quarter			Filing Date
Jan. 1	Feb. &	March 31	April 20, 1985
Feb. 1		April 30	May 20, 1985
March 1		May 31	June 20, 1985"

(Underscoring supplied)

For the reason that quarterly sales tax returns, are treated as non-cumulative, petitioner's tabulation of prescription (p. 8, Memorandum; p. 181, CTA rec.) is correctly presented. Respondent's right to assess the deficiency sales tax for the first three (3) quarters of 1985, had already prescribed, as more than three years had lapsed from the dates of filing the returns up to the date the assessment was issued. Only the right to assess the sales tax liability for the 4th quarter of 1985, did not prescribe.

However, such sales tax liability corresponding to the 4th quarter of 1985, cannot likewise be upheld by this Court, as its legal basis which is Revenue Regulations No. 19-84, is null and void, for it was not published in the Official Gazette as required by Article 2 of the New Civil Code. Petitioner presented Exh. "A-

1", which is a Certification issued by Mr. Heriberto Bacalla, the Chief of the Official Gazette Publication, attesting to the fact that Rev. Regs. No. 19-84 was not submitted to his office for publication in the Official Gazette. Citing the case of "Tañada vs. Tuvera", 146 SCRA 446, petitioner alleged that if the purpose of administrative rules and regulations is to enforce or implement existing law, such rules and regulations must be published in the Official Gazette to be valid. Respondent presented no evidence to rebut or contradict petitioner's Exhibit "A-1". She merely argued in her Memorandum, that Rev. Regs. No. 19-84 is only an interpretative regulation issued as a guideline to officers and employees of the Bureau of Internal Revenue (last par., p. 10, Memorandum of Resp.; p. 168, CTA rec.).

The Court cannot subscribe to respondent's argument. A careful perusal of Rev. Regs. No. 19-84 shows that although it is addressed to all B.I.R. officers and others concerned, it is more for the information and guidance of all manufacturer - taxpayers. To the Court's mind, the provisions of the regulations cater more to the latter's interest and therefore, requires publication not only in the Official Gazette but also in newspapers of general circulation, for wider dissemination of information, There being no publication in the Official Gazette which is mandatorily required pursuant to Article 2 of the New Civil Code, Rev. Regs. No. 19-84 is null and void. Consequently, the legal basis of the deficiency sales tax assessment for the 4th quarter of 1985 being void, it follows that the assessment is also not valid, and must be withdrawn or cancelled. With this declaration of nullity, a further discussion on the other side issues raised by both parties relative to the provisions of RR No. 19-84 is already moot and academic.

The Court now comes to a discussion of the third issue: whether or not petitioner is liable for payment of deficiency expanded withholding tax.

Respondent states in her Memorandum, first paragraph, page 7 thereof (p. 165, CTA rec.) that the basis of the deficiency withholding tax assessment is the payment made by PDCP to SMC pursuant to their Joint-Venture Agreement, Section 6.3 of which, provides as follows:

> "SMC shall provide such corporate and management services (including bookkeeping, auditing, accounting, computer and SMC officers services) and facilities (including the plant and office space as delineated and identified in the plan attached hereto as Schedule II) as and for as long as PDCP may require. For such services and facilities, PDCP shall reimburse SMC at cost, payable monthly in arrears, which is determined and agreed to be 7.5% of the revenue of PDCP."

The Court agrees with respondent's findings that the payments, made by petitioner to SMC for the corporate and management services rendered by the latter to the former, were service income on the part of SMC. Therefore, petitioner PDCP should have properly subjected to withholding the income payments to SMC.

The Court does not concur with petitioner's contention, that such income represents reimbursements for the actual cost or value of services rendered. The word "reimburse" as used in the Joint-Venture Agreement is incredible. For how can the monthly actual cost of services be determined in advance as to be equivalent to 7.5% of petitioner's revenue? Reimbursements, in common parlance, are by nature variable and cannot be pre-determined as fixed. Petitioner's payments, therefore, are service income on the part of SMC, subject to expanded withholding tax.

Moreover, the services rendered by SMC to petitioner are <u>management services</u>, as expressly stated in the Joint-Venture Agreement. It is a well-settled rule that:

> "xxx Management fees paid to a general manager is income of the latter, i.e. income payment to the manager for his professional services. Management fees belong to and are of the same class or nature as professional, promotional and talent fees, which are income payments and which are subject to expanded withholding tax (Section 1, pars. (a) and (b) of Revenue Regulations No. 13-78)." (See

"Anscor Container Corp. vs. CIR and CTA", CA-G.R. SP No. 22912, March 21, 1991 as cited in CTA Case No. 4233, "PBP Financing and Leasing Corporation vs. CIR", promulgated on October 24, 1994).

WHEREFORE, in view of the findings: 1. that the deficiency sales tax assessment has already prescribed and has been issued not in accordance with law; and 2. that the deficiency expanded withholding tax assessment has been validly and/or legally issued; the Court hereby **ORDERS:**

a) respondent to **CANCEL** and/or **WITHDRAW** the 1985 deficiency sales tax assessment issued against petitioner in the total amount of P23,971,805.41; and

b) petitioner to **PAY** immediately the amount of P1,465,742.75 (P1,466,042.75 less P300.00.) as deficiency expanded withholding tax also for the year 1985. Compromise penalty cannot be imposed or collected without the agreement and conformity of the taxpayer (Wonder Mechanical Engineering Corporation vs. Court of Tax Appeals, L-22805 and 27858, June 30, 1975, 64 SCRA 555).

SO ORDERED.

ERNESTO D. ACOSTA
Presiding Judge

I CONCUR:

RAMON O. DE VEYRA
Associate Judge

CERTIFICATION

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

ERNESTO D. ACOSTA
Presiding Judge
Court of Tax Appeals