REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

EN BANC

MCDONALD'S PHILIPPINES REALTY CORPORATION, Petitioner,	**CTA EB NO. 1283** (CTA Case No. 8506)
- versus -	
COMMISSIONER OF INTERNAL REVENUE, Respondent.	**CTA EB NO. 1284** (CTA Case No. 8506)
x - x	
COMMISSIONER OF INTERNAL REVENUE, Petitioner,	Present: **DEL ROSARIO,** *P.J.*, **CASTAÑEDA, Jr., BAUTISTA, UY, CASANOVA, FABON-VICTORINO, MINDARO-GRULLA, RINGPIS-LIBAN,** *and* **MANAHAN,** *JJ.*
- versus -	
MCDONALD'S PHILIPPINES REALTY CORPORATION, Respondent.	Promulgated: FEB 09 2017 3:25 p.m.

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DECISION

RINGPIS-LIBAN, *J.*:

The Cases

Before the Court are the following:

1. Petition for Review,[1] docketed as CTA EB No. 1283, seeking:

   a) The reversal of the Decision[2] dated October 29, 2014 and Resolution[3] dated February 20 2015 in CTA Case No. 8506, entitled *McDonald's Philippines Realty Corporation v. Commissioner of Internal Revenue*, insofar as it ordered petitioner to pay respondent the amount of ₱3,698,006.76, representing the sum of the basic deficiency VAT for taxable year 2008 in the amount of ₱2,958,405.41 and the 25% surcharge imposed under Section 248(A)(3), Tax Code, in the amount of ₱739,601.35, plus deficiency interest and delinquency interest; and

   b) The cancellation and withdrawal of respondent's assessment for deficiency VAT for the CY ended December 31, 2008 in the aggregate amount of ₱10,194,107.65, inclusive of interest and surcharge; and

2. Petition for Review,[4] docketed as CTA EB No. 1284, praying that the Decision[5] promulgated on 29 October 2014, partially granting the Petition for Review in CTA Case No. 8506, entitled *McDonald's Philippines Realty Corporation v. Commissioner of Internal Revenue*, and the Resolution[6] promulgated on 20 February 2015 be reversed and set aside and a new one be rendered denying the original Petition for Review for utter lack of merit and to direct respondent to pay the amount of ₱10,194,107.65 as deficiency value added tax for calendar year ended December 31, 2008, plus 50% surcharge and 20% deficiency and delinquency interest until full payment pursuant to Sections 248 and 249 of the National Internal Revenue Code of 1997, as amended.

The Facts

The facts are summarized by the Court in Division, as follows:

> Mcdonald's Philippines Realty Corporation [(MPRC)] is a foreign corporation organized and existing under the Laws of Delaware, United States of America with license to do business through its Philippine branch located at 17th Floor Citibank Center

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1 Under Section 18 of Republic Act (R.A.) No. 1125, as amended by R.A. No. 9282.
2 Penned by Associate Justice Juanito C. Castañeda, Jr. with Associate Justice Caesar A. Casanova concurring. Docket (CTA EB No. 1283), pp. 44-82.
3 Penned by Associate Juanito C. Castañeda, Jr. with Associate Justices Caesar A. Casanova and Amelia R. Cotangco-Manalastas concurring. Docket (CTA EB No. 1283), pp. 83-88.
4 Under Section 3(b), Rule 8 of the Revised Rules of the Court of Tax Appeals.
5 Supra, note 2.
6 Supra, note 3.

Building, Paseo de Roxas, Salcedo Village, Makati City. It is a registered taxpayer of the Bureau of Internal Revenue ("BIR"), Large Taxpayers District Office as shown by its Certificate of Registration dated January 1, 1997 with Taxpayer's Identification Number ("TIN") 000-130-921-000.

On the other hand, the Commissioner of Internal Revenue [(CIR)] as a public official is tasked to decide disputed assessments, collection, refund of erroneously or excessively paid internal revenue taxes, fees or other charges, penalties, or other matters under the 1997 National Internal Revenue Code ("NIRC"), as amended, or other laws administered by the BIR.

[MPRC] established its Philippine branch office for the purpose of acquiring and leasing back two (2) existing Mcdonald's restaurants to Golden Arches Development Corporation ("GADC"), and developing new Mcdonald's restaurant sites which will then be leased to McGeorge Foods, Inc.

On October 18, 2011, [the CIR] through OIC-Assistant Commissioner Alfredo V. Misajon sent [MPRC] a preliminary assessment notice ("PAN") of its alleged 2008 value added tax ("VAT") deficiency of ₱7,422,438.30.

[The CIR] issued a formal assessment notice ("FAN") which was received by [MPRC] on November 22, 2011. In the FAN, [the CIR] informed [MPRC] of its alleged 2008 VAT deficiency of ₱7,438,096.98 inclusive of interest, detailed as follows:

Rentals and Interest Receivable, beg. (₱38,866,011.00 ÷ 1.12)		34,701,795.50
Add: Income during the year		
1. Rentals	38,776,417.00	
2. Interest	25,755,318.00	64,531,735.00
Total amount available for collection		99,233,530.50
Less: Rentals & Interest, Receivable, end. (₱26,005,282.00 ÷ 1.12)		23,219,001.78
Gross Receipts for the year 2008		76,014,528.72
Output VAT due		9,121,743.14
Less: creditable input tax		(31,134.00)
VAT payable per audit		9,090,609.14
Less: VAT payment		(4,392,863.68)
Basic deficiency VAT due		4,697,745.46
Add: 20% interest		2,740,351.52
Total		7,438,096.98

On December 22, 2011, [MPRC] protested the FAN.

On May 22, 2012, [MPRC] received a copy of the final decision on disputed assessment ("FDDA") dated April 25, 2012 reiterating [the CIR's] demand for payment of its alleged 2008 VAT deficiency and interest in the increased amount of ₱10,194,107.65 computed as follows:

Rentals and Interest Receivable, beg. (₱38,866,011.00 ÷ 1.12)		34,701,795.50
Add: Income during the year		
1. Rentals	38,776,417.00	
2. Interest	25,755,318.00	64,531,735.00
Total amount available for collection		99,233,530.50
Less: Rentals & Interest, Receivable, end. (₱26,005,282.00 ÷12)		(23,219,001.78)
Gross Receipts for the year 2008		76,014,528.72
Output VAT due		9,121,743.14
Less: creditable input tax		(31,134.00)
VAT payable per audit		9,090,609.14
Less: VAT payments		(4,392,863.68)
Basic deficiency VAT due		4,697,745.46
Add: 50% surcharge based on Section 248[B]		2,348,872. 73
20% interest from January 26, 2009 to May 31, 2012		3,147,489.46
Total		**10,194,107.65**

The FDDA is premised on the following grounds:

(a) The FAN was issued in accordance with existing law and regulations;

(b) There is substantial underdeclaration of gross receipts for taxable year 2008 which would warrant the extension of the prescriptive period up to ten (10) years;

(c) There is underpayment of VAT on rental income because [MPRC's] method of declaration of revenue per 2008 VAT returns is not on accrual basis;

> (d) [MPRC's] interest income is subject to VAT; and
>
> (e) The computation of [MPRCs] gross receipts subject to VAT was based on Revenue Administrative Memorandum Order No. 1-90.

Dissatisfied, [MPRC] filed before the Court of Tax Appeals Second Division ("Court in Division") a petition for review on June 21, 2012. [MPRC] seeks for the cancellation and withdrawal of [the CIR's] assessment for deficiency VAT of ₱10,194,107.65, inclusive of interest and surcharge for calendar year ("CY") ended December 31, 2008.

In response to the petition for review, [the CIR] in her answer countered that [MPRC] failed to substantiate or controvert by substantial evidence the BIR factual findings as shown under the Details of Discrepancies attached to the PAN, FAN and FDDA; that [MPRC] failed to subject to VAT its gross receipts relating to rental/interest income of ₱39,147,881.33; that [MPRC] is a lender investor for the past several years as reflected in its prior years' income tax returns and clearly earning yearly profits of ₱25,755,318.00 for the year 2008 which is 70% of the main income; that she complied with the due process requirement by stating the factual and legal bases in the issuance of the PAN, FAN and FDDA; that [MPRC] substantially underdeclared its gross receipts by more than 30% as declared in its VAT returns for year 2008; that assessment period is within ten (10) years from discovery of falsity or fraud when a taxpayer files "false or fraudulent returns"; that all presumptions are in favor of the correctness of the assessment and failure to present proof of error in the assessment will justify judicial affirmation of the assessment.

x x x

The parties jointly stipulated the following issues:

> 1. Whether or not [MPRC's] administrative and judicial protests against the deficiency VAT assessment for calendar year 2008 were filed within the periods prescribed under Section 228, Tax Code.
>
> 2. Whether or not the PAN, FAN and FDDA were issued in violation of the due process requirement under Section 228, Tax Code and Revenue Regulations No. 12-99.

> 3. Whether or not [the CIR's] right to assess [MPRC's] deficiency VAT liability for the first, second and third quarters of calendar year 2008 had already prescribed.
>
> 4. Whether or not [MPRC] failed to controvert by substantial evidence the BIR's factual findings, as shown in the Details of Discrepancies attached to the PAN, FAN/Formal Letter of Demand, and FDDA.
>
> 5. Whether or not [MPRC] underdeclared its rental income in its quarterly VAT returns for calendar year 2008.
>
> 6. Whether or not [MPRC's] interest income for calendar year 2008 is subject to VAT.
>
> 7. Whether or not [MPRC] substantially underdeclared its gross receipts by more than 30% as declared in its VAT returns for taxable year 2008 and, thus, rendered the subject VAT returns of [MPRC] for taxable year 2008 as "false or fraudulent returns" within the contemplation of Section 222 of the Tax Code.
>
> 8. Whether or not the imposition of a 50% surcharge on [MPRC's] alleged deficiency VAT for calendar year 2008 is valid.[7]

The Rulings of the Court in Division

The Court in Division partially granted MPRC's Petition for Review in the Decision[8] dated October 29, 2014 (assailed Decision), thus:

> **WHEREFORE**, premises considered, Petition for Review is **PARTIALLY GRANTED.** The Final Decision on Disputed Assessment issued by respondent against petitioner covering deficiency value-added tax for CY 2008 is partly upheld. Accordingly, petitioner should be ordered to pay respondent the amount of ₱3,698,006.76 representing the sum of the basic deficiency VAT for taxable year 2008 in the amount of

[7] Docket (CTA EB No. 1283), pp. 45-49.
[8] Supra, note 2.

₱2,958,405.41 and the 25% surcharge imposed under Section 248(A)(3) of the NIRC of 1997, in the amount of ₱739,601.35, as shown below:

Basic Deficiency VAT	₱ 2,958,405.41
Add: 25% Surcharge	739,601.35
TOTAL	**₱ 3,698,006. 76**

In addition, petitioner is liable to pay:

a) Deficiency interest at the rate of twenty percent (20%) per annum on the basic deficiency VAT of ₱2,958,405.41 computed from January 25, 2009, until full payment thereof pursuant to Section 249(B) of the 1997 NIRC, as amended; and

b) Delinquency interest at the rate of twenty percent (20%) per annum on the 20% deficiency interest which have accrued as aforestated in (a) and on the total amount of ₱3,698,006. 76, computed from May 22, 2012 until full payment thereof pursuant to Section 249(C) of the 1997 NIRC, as amended.

SO ORDERED.[9]

The Court in Division found that: (1) MPRC protested the FAN and appealed before the Court within the periods mandated by law;[10] (2) the PAN, FAN and FDDA are supported by factual and legal bases;[11] (3) MPRC duly reported its 2008 rental income;[12] (4) MPRC underdeclared substantial receipts from interest income on loans;[13] (5) false returns are assessed within ten years from discovery of the falsity;[14] and (6) 50% surcharge is invalid, instead, 25% surcharge should be imposed.[15]

Aggrieved, both MPRC and the CIR filed Motions for Partial Reconsideration, which the Court in Division denied in a Resolution[16] dated February 20, 2015 (assailed Resolution), thus:

[9] Docket (CTA EB No. 1283), pp. 80-81.
[10] Id. at pp. 49-51.
[11] Id. at pp. 51-55.
[12] Id. at pp. 58-67.
[13] Id. at pp. 67-76.
[14] Id. at pp. 55-58.
[15] Id. at pp. 76-80.
[16] Supra, note 3.

> **WHEREFORE**, premises considered, petitioner and respondent's Motions for Partial Reconsideration are hereby **DENIED** for lack of merit.[17]

Hence, these petitions.

MPRC filed a Motion for Extension of Time to file Petition for Review on March 13, 2015,[18] which the Court granted in a Resolution dated March 16, 2015.[19] Within the period granted, MPRC filed its Petition for Review on March 13, 2015,[20] docketed as CTA EB No. 1283. The Court ordered the CIR to comment on MPRC's petition in a Resolution dated May 5, 2015.[21]

Meanwhile, the CIR filed a Motion for Extension of Time to file Petition for Review on March 16, 2015,[22] which the Court granted in a Resolution dated March 17, 2015.[23] Within the period granted, the CIR filed his Petition for Review on April 1, 2015,[24] docketed as CTA EB No. 1284.

On May 11, 2015, the Court resolved to consolidate CTA EB No. 1284 with CTA EB No. 1283, considering that the Petitions for review are appeals from the Decision and Resolution of the Court in Division in the same case.[25]

On June 1, 2015, in relation to CTA EB No. 1283, the CIR filed a Motion for Extension of Time to File Comment (To Petitioner's Petition for Review),[26] which the Court granted.[27] However, the CIR failed to file his comment.[28]

On September 1, 2015, the Court ordered MPRC to file its Comment on the CIR's Petition for Review in CTA EB No. 1284.[29] MPRC filed a Motion for Extension of Time to File Comment on September 28, 2015,[30] which the Court granted on October 1, 2015.[31] Within the extension period granted, MPRC filed its Comment (Re: Petition for Review dated April 1, 2015) on October 5, 2015.[32]

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[17] Id. at p. 88.
[18] Id. pp. 1-4.
[19] Id. at p. 6.
[20] Id. at pp. 7-38.
[21] Id. at pp. 90-91.
[22] Docket (CTA EB No. 1284), pp. 1-4.
[23] Id. at p. 6.
[24] Id. at pp. 8-18.
[25] Docket (CTA EB No. 1283), p. 92.
[26] Id. at pp. 93-95.
[27] Id. at p. 97.
[28] Id. at p. 102. Records Verification Report dated July 20, 2015 of the Judicial Records Division.
[29] Id. at pp. 100-101.
[30] Id. at pp.103-105.
[31] Id. at p. 106.
[32] Id. at pp. 107-115.

On November 11, 2015, the Court gave due course to the petitions and ordered the parties to submit their respective memoranda.[33]

On December 28, 2015, the CIR filed a Manifestation stating that he is adopting his Petition for Review as his Memorandum. On the other hand, MPRC filed its Memorandum on January 25, 2016,[34] within the extension period granted.[35]

Hence, on February 11, 2016, the Court issued a Resolution submitting the consolidated cases for decision.[36]

The Issues

MPRC raised the following issues in CTA EB No. 1283:

1. Petitioner respectfully submits that the Decision and the Resolution are erroneous based on the following grounds:

    a. The CTA-Division erred in holding that respondent can validly assess within the 10-year prescriptive period even if respondent's Preliminary Assessment Notice (PAN) and Final Assessment Notice (FAN) did not allege that petitioner's Quarterly VAT Returns for CY 2008 were fraudulent or false. Respondent only invoked the extraordinary 10-year prescription period in her Final Decision on Disputed Assessment (FDDA) after petitioner argued that the deficiency VAT assessment for CY 2008 had already prescribed pursuant to Section 203, Tax Code.

    b. The extraordinary 10-year prescription period does not apply in this case because petitioner's Quarterly VAT Returns for CY 2008 may not be considered "false returns" as contemplated under Section 222(a), Tax Code.

    c. The pronouncements of the Supreme Court in Aznar v. Court of Tax Appeals (Aznar) should be read in light of the particular factual milieu of the case, where after the application of the net worth and expenditures method of tax investigation, the Court found that there was

[33] Id. at pp. 118-120.
[34] Id. at pp. 134-184.
[35] Id. at pp. 132-133.
[36] Id. at pp. 186-187.

concealment of income which placed the government at a disadvantage "so as to prevent its lawful agents from proper assessment of tax liabilities." In view thereof, the Supreme Court applied the extraordinary 10-year prescription period from the time of the discovery of the falsity, fraud, or omission in order to protect the government's interest. In the case at bar, it is established that petitioner did not conceal its interest income, as it was clearly shown in its income tax return (ITR) and audited financial statements (AFS). As such, there is no justification for the application of the extraordinary 10-year prescription period in this case because the government was not in any way placed at a disadvantage or prevented from assessing the correct amount of tax.

d. In order to render a return made by a taxpayer a "false return" within the meaning of Section 222, Tax Code, there must appear a design to mislead or deceive on the part of the taxpayer, or at least culpable negligence.

e. Applying the *ejusdem generis* rule in statutory construction, the falsity of the return in Section 222(a), Tax Code, should be construed as referring to a false return that it is akin to a fraudulent return with intent to evade tax, or tantamount to the non-filing of a return.

f. The application of the extraordinary 10-year prescription period under Section 222(a), Tax Code, in case of any error or omission in the taxpayer's tax return would render inoperative the ordinary 3-year prescription period provided under Section 203, Tax Code, since all deficiency tax assessments would spring from an error in the return.

2. Based on the foregoing, petitioner respectfully submits that respondent has already lost her right to assess petitioner's deficiency VAT for the 1^{st}, 2^{nd}, and 3^{rd} quarters of CY 2008.

3. Furthermore, the CTA-Division erred in its ruling that the interest income derived by petitioner from the unpaid rentals and the loan that it granted to GADC was incidental to its leasing business and is, therefore, subject to VAT pursuant to Section 105, in relation to Section 108(A), Tax Code. With all due respect, petitioner respectfully submits that the CTA-Division's ruling is erroneous inasmuch as the rulings in CS Garments, Inc. v. CIR (CS Garments) and Lapanday Foods

> Corporation v. CIR (Lapanday) cited by the CTA-Division are inapplicable to petitioner's case.[37] *(Underscoring in the original.)*

On the other hand, the CIR, in CTA EB No. 1284, assigned the following errors:

> The Honorable Court erred in denying the imposition of the 50% surcharge.
>
> The Honorable Court erred in ruling that petitioner fully paid and remitted its VAT payment for rental income.[38]

The Ruling of the Court

We deny the petitions.

At the outset, we note that the issues raised by MPRC and the CIR are rehashed from their arguments before the Court in Division, and have been sufficiently discussed in the assailed Decision and assailed Resolution.

CTA EB No. 1283

On the Prescriptive Period for Issuing the Assessment

Pertinent to MPRC's argument that the assessment was issued beyond the prescriptive period are Sections 203 and 222 of the 1997 NIRC, as amended. Section 203 provides the general rule that internal revenue taxes shall be assessed within three years after the last day prescribed by law for filing the same, thus:

> 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.

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[37] Docket (CTA EB No. 1283), pp. 12-13.
[38] Docket (CTA EB No. 1284), p. 13.

The three-year prescriptive period for issuing an assessment provides for exceptions, such as paragraph (a) of Section 222 of the 1997 NIRC, as amended, which reads:

> SEC. 222. Exceptions as to Period of Limitation of Assessment and Collection of Taxes. –
>
> (a) In the case of a false or fraudulent return with intent to evade tax or failure to file a return, the tax may be assessed, or a proceeding in court for the collection of such tax may be filed without assessment, at any time within ten (10) years after the discovery of the falsity, fraud or omission: *Provided*, That in a fraud assessment which has become final and executory, the fact of fraud shall be judicially taken cognizance of in the civil or criminal action for the collection thereof.

Hence, in the case of a false or fraudulent return with intent to evade tax or failure to file a return, the tax may be assessed at any time within ten years after the discovery of the falsity, fraud or omission. The Supreme Court, in *Aznar v. Court of Tax Appeals*,[39] discussed the difference between a "false return" and a "fraudulent return", as follows:

> x x x We believe that the proper and reasonable interpretation of said provision should be that in the three different cases of (1) false return, (2) fraudulent return with intent to evade tax, (3) failure to file a return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within ten years after the discovery of the (1) falsity, (2) fraud, (3) omission. Our stand that the law should be interpreted to mean a separation of the three different situations of false return, fraudulent return with intent to evade tax, and failure to file a return is strengthened immeasurably by the last portion of the provision which segregates the situations into three different classes, namely, "falsity", "fraud" and "omission." **That there is a difference between "false return" and "fraudulent return" cannot be denied. While <u>the first merely implies deviation from the truth, whether intentional or not, the second implies intentional or deceitful entry with intent to evade the taxes due.</u>** *(Emphasis and underscoring supplied.)*

Based on the foregoing, a return is false as long as there is a deviation from the truth, whether intentional or not. In the instant case, the Court in Division correctly found that there was falsity in MPRC's 2008 Quarterly VAT

[39] G.R. No. L-20569, August 23, 1974.

Returns for not declaring substantial receipts from its interest income in the amount of ₱24,653,378.41.

Still, MPRC insists that *Aznar* was not properly applied by the Court in Division. Citing the Court of Appeals decision in *CIR v. Ayala Hotels, Inc.*,[40] MPRC claims that only "false returns" filed with the intent to evade tax would call for the application of Section 222 of the 1997 NIRC.[41]

However, the Court of Appeals' pronouncement in *Ayala* cannot modify the Supreme Court's ruling in *Aznar*. In the hierarchy of courts in this jurisdiction, the Supreme Court is supreme. In fact, any doctrine or principle of law laid down by the Supreme Court, either rendered *en banc* or in division, may be overturned or reversed only by the Supreme Court sitting *en banc*.[42]

Consequently, pursuant to *Aznar*, the ten-year prescriptive period is applicable in this case. MPRC received the FAN on November 22, 2011; hence, the assessment was made within the prescriptive period provided by law.

On the Interest Income from Unpaid Rentals and Loan

MPRC argues that the Court in Division erred in holding that interest income it derived from its loan to GADC and the unpaid rentals from GADC were incidental to its leasing business and is therefore a transaction made in the course of trade or business.[43]

We do not agree.

In *Mindanao II Geothermal Partnership v. Commissioner of Internal Revenue*,[44] the Supreme Court interpreted the meaning of an "incidental" transaction, thus:

> Mindanao II asserts that the sale of a fully depreciated Nissan Patrol is not an incidental transaction in the course of its business; hence, it is an isolated transaction that should not have been subject to 10% VAT.
>
> Section 105 of the 1997 Tax Code does not support Mindanao II's position:

[40] CA-G.R. No. 70025, April 19, 2004.
[41] Docket (CTA EB No. 1283), pp. 22-25.
[42] Section 4(3), Article VIII of the 1987 Constitution.
[43] Docket (CTA EB No. 1283), pp. 31-36.
[44] G.R. Nos. 193301 & 194637, March 11, 2013.

> SEC. 105. Persons Liable. — Any person who, in the course of trade or business, sells barters, exchanges, leases goods or properties, renders services, and any person who imports goods shall be subject to the value-added tax (VAT) imposed in Sections 106 to 108 of this Code.
>
> The value-added tax is an indirect tax and the amount of tax may be shifted or passed on to the buyer, transferee or lessee of the goods, properties or services. This rule shall likewise apply to existing contracts of sale or lease of goods, properties or services at the time of the effectivity of Republic Act No. 7716.
>
> The phrase "in the course of trade or business" means the regular conduct or pursuit of a commercial or an economic activity, including transactions incidental thereto, by any person regardless of whether or not the person engaged therein is a nonstock, nonprofit private organization (irrespective of the disposition of its net income and whether or not it sells exclusively to members or their guests), or government entity.
>
> The rule of regularity, to the contrary notwithstanding, services as defined in this Code rendered in the Philippines by nonresident foreign persons shall be considered as being rendered in the course of trade or business.

Mindanao II relies on *Commissioner of Internal Revenue v. Magsaysay Lines, Inc. (Magsaysay)* and *Imperial v. Collector of Internal Revenue (Imperial)* to justify its position. *Magsaysay*, decided under the NIRC of 1986, involved the sale of vessels of the National Development Company (NDC) to Magsaysay Lines, Inc. We ruled that the sale of vessels was not in the course of NDC's trade or business as it was involuntary and made pursuant to the Government's policy for privatization. *Magsaysay*, in quoting from the CTA's decision, imputed upon *Imperial* the definition of "carrying on business." *Imperial*, however, is an unreported case that merely stated that "'to engage' is to embark in a business or to employ oneself therein."

Mindanao II's sale of the Nissan Patrol is said to be an isolated transaction. However, it does not follow that an isolated

transaction cannot be an incidental transaction for purposes of VAT liability. **Indeed, a reading of Section 105 of the 1997 Tax Code would show that a transaction "in the course of trade or business" includes "transactions incidental thereto." Mindanao II's business is to convert the steam supplied to it by PNOC-EDC into electricity and to deliver the electricity to NPC. In the course of its business, Mindanao II bought and eventually sold a Nissan Patrol. Prior to the sale, the Nissan Patrol was part of Mindanao II's property, plant, and equipment. Therefore, the sale of the Nissan Patrol is an incidental transaction made in the course of Mindanao II's business which should be liable for VAT.**
(Citations omitted. Emphasis supplied.)

Hence, the Court in Division was correct when it ruled as follows:

In the case of *CS Garments, Inc. v. Commissioner of Internal Revenue*, this Court held that although the primary business of CS Garments is the manufacturing of garments for sale abroad, the sale of motor vehicle to its general manager is considered an incidental transaction subject to VAT as it was purchased and used in carrying out petitioner's business x x x.

x x x

Similarly, in the case of *Lapanday Foods Corporation v. Commissioner of Internal Revenue*, this Court ruled that if the income from the main business activity is subject to VAT, the incidental income shall also be subject to VAT, provided that there is no particular provision applicable to the specific transaction.

Here, the financial statements for the years ended December 31, 2008 and 2007 disclose that the subject interest income arose from the following two (2) loan/debt agreements with its lone client, GADC, to be allocated for the acquisition of real properties and unpaid rentals.

1. **Related Party Transactions**

   a. xxx xxx xxx

   b. On March 17, 2005, the Branch entered into a loan agreement with GADC covering interest-bearing, long term advances granted to GADC in prior years <u>for land and equipment purchased for various</u>

restaurants and warehouse amounting to P57,431,435. The loan is payable in full on March 17, 2009. Interest on the loan shall accrue at 8.4375% from March 1, 2005 to March 17, 2006; thereafter, interest shall accrue at six-month PHIBOR rate plus 2%, which the Branch will reset on March 18 of each year.

On the same date, the Branch and GADC signed an Acknowledgment of Debt Agreement, whereby GADC acknowledged that it has **unpaid rentals** and interest due to the Branch amounting to ₱366,712,722 ("receivable"'). In accordance with the terms of the said agreement, GADC executed a Promissory Note in favor of the Branch for ₱366,712,722, which is payable in full on March 17, 2009. Interest on the receivable shall accrue at 8.4375% from March 1, 2005 to March 17, 2006; thereafter, the interest shall accrue at six-month PHIBOR rate plus 2%, which the Branch will reset on March 18 of each *year.*

Relative to the loan amount of ₱57,431,435.38, the utilization of the proceeds thereof was clearly set forth in the Loan Agreement entered into by petitioner with GADC on March 17, 2005, thus:

> WHEREAS, **MPRC loaned GADC an amount of money for the period 16 July 1985 to 14 June 1991 to assist GADC in its purchase of real properties in the Philippines;**
>
> WHEREAS, GADC acknowledges the existence of the loan and receipt thereof from MPRC and the use of the proceeds thereof to purchase real properties located in the Philippines and more specifically described in Annex "A" of this Agreement;
>
> WHEREAS, **GADC has since developed some of the real properties as sites for McDonald's Restaurants, while one property was used to establish a distribution and supply warehouse;** and
>
> WHEREAS, while the real properties described in Annex "A" were sold by GADC in 2002

> to another corporation, Golden Arches Realty Corporation, **the McDonald's Restaurants, as well as the distribution and supply warehouse located therein, remain the properties of GADC.**

Considering that petitioner established its branch office in the Philippines for the purpose of purchasing and leasing back two (2) existing McDonald's Restaurants to GADC and developing new McDonald's Restaurant sites which will then be leased to McGeorge Foods, Inc. as stated in its License to Transact Business in the Philippines issued by the SEC on November 12, 1984, it can be safely concluded that the loan it granted to GADC in the amount of ₱57,431,435.38 was in the pursuit of its leasing business with GADC. Consequently, the interest income it derived from the said loan, being incidental to its leasing business, is deemed a transaction "in the course of trade and business" which is subject to VAT pursuant to Section 105 in relation to Section 108(A) of the NIRC of 1997, as amended.

The same holds true with regard to GADC's debt to petitioner in the amount of ₱366,712,722. The Acknowledgement of Debt executed by petitioner and GADC on March 17, 2005 states that:

> WHEREAS, MPRC owns the leasehold improvements and the equipment, seating, signage and design of McDonald's Restaurants owned and operated by GADC which restaurants are listed in Annex "A" attached thereto;
>
> WHEREAS, MPRC also owns the leasehold improvements and equipment in the distribution and supply warehouse located at Marikina City, Philippines;
>
> WHEREAS, MPRC leased the above leasehold improvements and the equipment seating, signage and design to GADC in return for payment of lease/rental fees; and
>
> WHEREAS, to date, GADC has unpaid rentals due MPRC.
>
> Article I - Amount of the Receivables

> Upon and subject to the terms and conditions of this Agreement, GADC hereby acknowledges that it has unpaid rentals and unpaid interest due to MPRC in the amount of THREE HUNDRED SIXTY-SIX MILLION SEVEN HUNDRED TWELVE THOUSAND SEVEN HUNDRED TWENTY-ONE PHILIPPINE PESOS AND SEVENTY-NINE PHILIPPINE CENTAVOS (Php366,712,721.79), xxx

Evidently, from the foregoing, the interest income derived by petitioner from GADC's unpaid rentals, is considered a transaction made in the course of petitioner's lease business, and is subject to VAT pursuant to Section 105 in relation to Section 108(A) of the NIRC of 1997, as amended. *(Citations omitted. Emphasis and underscoring in the original.)*

<u>CTA EB No. 1284</u>

On the Surcharge Imposed

Section 248 of the 1997 NIRC, as amended, provides the civil penalties imposable, as follows:

> SEC. 248. Civil Penalties. – (A) There shall be imposed, in addition to the tax required to be paid, a penalty equivalent to twenty-five percent (25%) of the amount due, in the following cases:
>
> (1) Failure to file any return and pay the tax due thereon as required under the provisions of this Code or rules and regulations on the date prescribed; or
> (2) Unless otherwise authorized by the Commissioner, filing a return with an internal revenue officer other than those with whom the return is required to be filed; or
> (3) Failure to pay the deficiency tax within the time prescribed for its payment in the notice of assessment; or
> (4) Failure to pay the full or part of the amount of tax shown on any return required to be filed under the provisions of this Code or rules and regulations, or the full amount of tax due for which no return is required to be filed, on or before the date prescribed for its payment.

> (B) In case of willful neglect to file the return within the period prescribed by this Code or by rules and regulations, or in case a false or fraudulent return is willfully made, the penalty imposed shall be fifty percent (50%) of the tax or of the deficiency tax, in case any payment has been made on the basis of such return before the discovery of the falsity or fraud: *Provided*, That a substantial underdeclaration of taxable sales, receipts or income, or a substantial overstatement of deductions as determined by the Commissioner pursuant to the rules and regulations to be promulgated by the Secretary of Finance, shall constitute *prima facie* evidence of a false or fraudulent return: *Provided*, That failure to report sales, receipts or income in an amount exceeding thirty percent (30%) of actual deductions, shall render the taxpayer liable for substantial underdeclaration of sales, receipts or income or fore overstatement of deductions, as mentioned herein.

In *Aznar*, the Supreme Court declared that the imposition of the fifty percent fraud penalty under the then Section 72 of the Tax Code[45] is improper, in the absence of a willful intent to evade tax:

> The lower court's conclusion regarding the existence of fraudulent intent to evade payment of taxes was based merely on a presumption and not on evidence establishing a willful filing of false and fraudulent returns so as to warrant the imposition of the fraud penalty. The fraud contemplated by law is actual and not constructive. It must be intentional fraud, consisting of deception willfully and deliberately done or resorted to in order to induce another to give up some legal right. Negligence, whether slight or gross, is not equivalent to the fraud with intent to evade the tax contemplated by the law. It must amount to intentional wrong-doing with the sole object of avoiding the tax. It necessarily follows that a mere mistake cannot be considered as fraudulent intent, and if both petitioner and respondent Commissioner of Internal Revenue committed mistakes in making entries in the returns and in the assessment, respectively, under the inventory method of determining tax liability, it would be unfair to treat the mistakes of the petitioner as tainted with fraud and those of respondent make in good faith.
>
> **We conclude that the 50% surcharge as fraud penalty authorized under Section 72 of the Tax Code should not be**

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[45] SEC. 72. *Surcharges for failure to render returns and for rendering false and fraudulent returns.* – In case of willful neglect to file the return or list required under this Title within the time prescribed by law, of in the case a false or fraudulent return or list is willfully made, the Commissioner of Internal Revenue shall add to the tax or to the deficiency tax, in case any payment has been made on the basis of such return before the discovery of the falsity or fraud, a surcharge of fifty per centum of the amount of such tax or deficiency tax.

> **imposed, but eliminated from the income tax deficiency for each year from 1946 to 1951, inclusive.**[46]

Hence, the Court in Division correctly held that –

> In the *Aznar* case, the Supreme Court ruled that where there is a deviation from the truth, whether intentional or not, the ten-year prescriptive period to assess should be applied. At the same time, the High Court ruled that there is no basis for the imposition of the fifty percent (50%) fraud penalty in the absence of a willful fraudulent act on the part of the taxpayer x x x.
>
> x x x
>
> Applying the rationale laid down by the Supreme Court in the *Aznar* case, the 50% surcharge imposed by the [CIR] in the present case is improper, and, thus, must be cancelled and withdrawn. However, the Court imposes surcharge of 25% pursuant to Section 248(A)(3) of the 1997 NIRC, as amended, for "failure to pay the deficiency tax within the time prescribed for its payment in the notice of assessment".
>
> **The underdeclaration in [MPRC]'s gross receipts on interest income for the CY 2008 did not arise from a deliberate attempt on its part to evade tax but on the honest belief that it is not subject to VAT.** This is supported by the fact that the interest income amounting to ₱25,755,318.00, as well as the rental and interest receivables as of December 31, 2007 and 2008 in the respective amounts of ₱38,866,011.00 and ₱26,005,282.00 used by the [CIR] in computing the deficiency VAT assessment are **disclosed in [MPRC]'s Audited Financial Statements for the years ended December 31, 2008 and 2007 and 2008 Annual Income Tax Return.** Thus, [the CIR] was not prevented from assessing the VAT on [MPRC]'s gross receipts from interest income for the CY 2008.[47]

Therefore, the 25% surcharge provided in Section 248(A) of the 1997 NIRC, as amended, instead of the 50% surcharge in Section 248(B) thereof, was properly imposed by the Court in Division.

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[46] Supra, note 39.
[47] Docket (CTA EB No. 1284), pp. 54-57.

On the VAT Payment for Rental Income

The CIR insists that MPRC has not fully paid and remitted its VAT for rental income. He claims that the Court in Division erred in dividing the rental receivables by 1.07 instead of 1.12. The CIR's position is untenable.

The assailed Decision discussed in detail that the use of 1.07 as a divisor is borne by the fact that MPRC records its receivables with the 5% expanded withholding tax already deducted. The discussion, found in pages 15 to 24 of the assailed Decision,[48] is painstakingly detailed and extensively references the exhibits on record. The CIR's insistence on the use of 1.12 as a divisor is clearly misplaced.

The CIR also takes issue with the finding of the Court in Division that the advanced VAT payments in 2007 was properly substantiated in order to be considered as VAT payments for the year 2008. The CIR insists that: (1) the advanced VAT payment in 2007 should not be considered as VAT payment for the year 2008; and (2) said finding requires further documentation, in particular, the CIR claims that the only evidence presented by MPRC was the amended Quarterly VAT Return for the fourth quarter of 2007.

The CIR's contention is untenable.

First, the record shows that when MPRC amended its Quarterly return for the fourth quarter of 2007, it included output VAT corresponding to rent income <u>received only on July 25, 2008</u>. The Court in Division held –

> The difference for the third quarter of CY 2008 in the amount of ₱13,013,954.66 excluding VAT and withholding tax pertains to the **actual cash collection received on July 25, 2008 as supported by OR No. 0106**[49] for the rent rebuild stores for 2006 and 2007. Accrual of rent rebuild was **recorded in the books on February 27, 2008 with General Journal 02629**[50] **<u>for posting in the accounting period of 2007</u>** x x x.[51] *(Emphasis and underscoring supplied.)*

The CIR's position will result in an unjust situation where MPRC will be required to make a second payment of the same output VAT, despite evidence that it was already paid.

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[48] Docket (CTA EB No. 1284), pp. 36-45.
[49] Exhibit "KKK-10".
[50] Exhibit "WWW".
[51] Id. at p. 42.

Second, the discussion in the assailed Decision, as well as in the assailed Resolution, is replete with references to numerous exhibits, that precisely support the Court in Division's findings. Pertaining to the particular claim of the CIR that the remittance to the BIR was not substantiated, the Court in Division held –

> Contrary to respondent's assertion, the amended Quarterly VAT return for the fourth quarter of 2007 showed that the amount of ₱1,680,056.96 pertaining to output VAT on rent income for the rent rebuild stores for 2006 and 2007 was paid in advance on March 26, 2008. **The VAT return supported by payment transaction number 80501312 for filing reference number 100800002143254,[52] is sufficient proof of payment and remittance to the BIR.** The tax return is the best evidence to determine whether proper taxes have been assessed and paid.[53] *(Emphasis and underscoring supplied.)*

In sum, it has been sufficiently shown that the deficiency VAT assessment for rental income was based on the CIR's mistaken use of 1.12 in dividing MPRC's receivables and the CIR's refusal to acknowledge that the amount of ₱1,680,056.96 pertaining to output VAT on rent income for the rent rebuild stores for 2006 and 2007 was indeed paid in advance, despite being supported by evidence. Hence, the Court in Division did not err in holding that MPRC had established that it paid the VAT on all of its gross receipts on rental income.

WHEREFORE, premises considered, the Court hereby **DENIES** the instant Petitions for lack of merit. The Decision dated October 29, 2014 and the Resolution dated February 20, 2015 of the Court in Division in CTA Case No. 8506 are hereby **AFFIRMED**.

SO ORDERED.

MA. BELEN M. RINGPIS-LIBAN
Associate Justice

WE CONCUR:

(See Dissenting Opinion)
ROMAN G. DEL ROSARIO
Presiding Justice

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[52] Exhibit "VVV-2".
[53] Docket (CTA EB No. 1284), p. 65.

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Associate Justice

(See Dissenting Opinion)
LOVELL R. BAUTISTA
Associate Justice

(See Concurring and Dissenting Opinion)
ERLINDA P. UY
Associate Justice

CAESAR A. CASANOVA
Associate Justice

ESPERANZA R. FABON-VICTORINO
Associate Justice

Cielito N. Mindaro-Grulla
CIELITO N. MINDARO-GRULLA
Associate Justice

Catherine T. Manahan
(See Dissenting Opinion)
CATHERINE T. MANAHAN
Associate Justice

CERTIFICATION

Pursuant to *Section 13 of Article VIII of the Constitution*, 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.

ROMAN G. DEL ROSARIO
Presiding Justice

REPUBLIC OF THE PHILIPPINES
Court of Tax Appeals
QUEZON CITY

EN BANC

MCDONALD'S PHILIPPINES REALTY CORPORATION,
Petitioner,

- *versus* -

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

CTA EB NO. 1283
(CTA Case No. 8506)

x- x

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

- versus -

MCDONALD'S PHILIPPINES REALTY CORPORATION,
Respondent.

CTA EB NO. 1284
(CTA Case No. 8506)

Members:

Del Rosario, ***P.J.,***
Castañeda, Jr.,
Bautista,
Uy,
Casanova,
Fabon-Victorino,
Mindaro-Grulla,
Ringpis-Liban, and
Manahan, ***JJ.***

Promulgated:

FEB 09 2017 3:25 p.m.

x- -x

DISSENTING OPINION

DEL ROSARIO, P.J.:

With due respect, I agree with the position taken by our learned colleague, Associate Justice Catherine T. Manahan, that **the ten-**

year prescriptive period to assess deficiency taxes under Section 222 (a) of the National Internal Revenue Code (NIRC) of 1997, as amended, **should not be applied in all cases involving false returns**.

As eloquently stated by Associated Justice Manahan in her Dissenting Opinion, the definition of a false return in ***Aznar vs. Court of Tax Appeals***[1] should be revisited in light of the Supreme Court's pronouncement in ***Commissioner of Internal Revenue vs. B.F. Goodrich Phils. Inc.***[2] wherein the Supreme Court did not consider mere deviation from truth as sufficient justification to consider the return as false for purposes of applying the ten-year prescriptive period to assess.

In this regard, I quote hereunder the position I have taken in ***Visayas Geothermal Company vs. Commissioner of Internal Revenue***[3] regarding the application of the ten-year prescriptive period to assess in case of false returns, *viz.*:

> "By way of obiter, however, I wish to state my humble view that in cases of false returns with no intent to evade tax, **<u>but due only to plain oversight, negligence or mistake</u>**, the three (3)-year prescriptive period under Section 203 of the NIRC of 1997, as amended, should apply.
>
> In this regard, I respectfully submit that the doctrine laid down in the *Aznar case* must be revisited in order to come up with a proper interpretation and application of the said provision, specifically, on the applicability of the ten-year prescriptive period in cases where the taxpayer's return is found to be false. It must be stressed that a careful application of Section 222 of the NIRC of 1997, as amended, is important to safeguard the rights of the taxpayers against the limitless taxing power of the government.
>
> Section 222 of the NIRC of 1997, as amended, originated from Section 332 (a) of the NIRC of 1939, which was lifted from Section 276 (a) of the Internal Revenue Code of 1939 of the United States of America.

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[1] G.R. No. L-20569, August 23, 1974.
[2] G.R. No. 104171, February 24, 1999.
[3] CTA Case No. 8425, Concurring Opinion in the Resolution dated March 16, 2015.

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When Presidential Decree No. 1158 was enacted into law, Section 332 (a) of the NIRC of 1939 was adopted as Section 223 (a) of the NIRC of 1977, as follows:

> 'Sec. 223. Exceptions as to period of limitation of assessment and collection of taxes. — (a) In the case of false or fraudulent return with intent to evade tax or of failure to file a return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within the ten years after the discovery of the falsity, fraud or omission: Provided, That in a fraud assessment which has become final and executory, the fact of fraud shall be judicially taken cognizance of the civil or criminal action for the collection thereof.'

With the enactment of Republic Act No. 8424, otherwise known as National Internal Revenue Code of 1997, Section 222 (a) restated Section 223 (a) of the NIRC of 1977, as follows:

> 'Sec. 222. Exceptions as to period of limitation of assessment and collection of taxes. — (a) In the case of false or fraudulent return with intent to evade tax or of failure to file a return, the tax may be assessed, or a proceeding in court for the collection of such tax may be filed without assessment, at any time within the ten years after the discovery of the falsity, fraud or omission: Provided, That in a fraud assessment which has become final and executory, the fact of fraud shall be judicially taken cognizance of in the civil or criminal action for the collection thereof.'

After a careful reading of the afore-cited Section 222 of the NIRC of 1997, as amended, I am of the opinion that the phrase 'with intent to evade tax' does not only apply to cases of fraudulent returns, but also to cases of false returns. This is evident by the fact that **no comma** was placed between the words '*[i]n the case of false*' and the words '*or fraudulent return with intent to evade tax*'. This clearly shows that the phrase '*with intent to evade tax*' modifies not only the words '*fraudulent return*' but also the word '*false*'.

Moreover, American jurisprudence on the matter, although merely persuasive as sizeable portion of the

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Philippine Tax Code is lifted from the United States Internal Revenue Code, is instructive:

1) **It is not sufficient that the return filed be false if, in fact, there exists no intent to evade any tax**. Thus, the mere fact that the inadequacy of the taxpayer's bookkeeping system causes a false return to be filed does not prevent the running of the statute where no concealment of any kind has been attempted and falsity has not knowingly been indulged in to evade the tax; and,

2) It has been held [that] where the taxpayer made no disclosure of a transaction on which he made a profit, his return was false with intent to evade the tax and that such tax could be assessed after the expiration of the usual period of limitation.

Indubitably, the filing of a false return must be coupled with intent to evade tax in order for the usual period of limitation not to apply. Applying this to Section 222 of the NIRC of 1997, as amended, a false return must have been made with intent to evade tax in order for the ten (10)-year prescriptive period to apply.

The application of the ten-year prescriptive period to assess even to situations involving false tax returns, <u>without intent to evade tax</u> on the part of the taxpayer, would render lifeless the three-year prescriptive period to assess under Section 203 of the NIRC of 1997, as amended, for practically all deficiency tax assessments involve entries in the return that are necessarily false. It will result in an absurd situation wherein the ten-year prescriptive period will be the usual period of limitation instead of the three-year prescriptive period. Such application will run counter to the Supreme Court's categorical pronouncement in **Republic of the Philippines v. Ablaza**, *viz.*:

> 'The law on prescription being a remedial measure should be **interpreted in a way conducive to bringing about the beneficent purpose of affording protection to the taxpayer** within the contemplation of the Commission which recommend[ed] the approval of the law.' (Emphasis supplied)" (Citations omitted)

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All told, I VOTE to **DENY** the Petition for Review filed by the Commissioner of Internal Revenue in CTA EB No. 1284. On the other hand, I VOTE to **GRANT** the Petition for Review filed by McDonald's Philippines Realty Corporation in CTA EB No. 1283 on the ground that the right of the Commissioner of Internal Revenue to assess it for deficiency Value-Added Tax (VAT) for taxable year 2008 has already prescribed.

ROMAN G. DEL ROSARIO
Presiding Justice

REPUBLIC OF THE PHILIPPINES
Court of Tax Appeals
QUEZON CITY

En Banc

MCDONALD'S PHILIPPINES REALTY CORPORATION, *Petitioner,*	**CTA *EB* No. 1283** (CTA Case No. 8506)
-versus-	
COMMISSIONER OF INTERNAL REVENUE, *Respondent.*	

x---x

COMMISSIONER OF INTERNAL REVENUE, *Petitioner,*	**CTA *EB* No. 1284** (CTA Case No. 8506)
-versus-	Present: ***Del Rosario, P.J. Castañeda, Jr., Bautista, Uy, Casanova, Fabon-Victorino, Mindaro-Grulla, Ringpis-Liban,*** *and* ***Manahan, JJ.***
MCDONALD'S PHILIPPINES REALTY CORPORATION *Respondent.*	Promulgated: FEB 09 2017 3:25 p.m.

x---x

DISSENTING OPINION

BAUTISTA, J.:

With due reverence to the *ponente,* I respectfully disagree with the application of the ten (10) year period to assess under *Section 222(a) of the 1997 National Internal Revenue Code ("1997 NIRC").* Instead, I humbly concur with the Dissenting Opinion of Associate Justice Manahan relating to her statement that the ten (10) year period does not apply to every false return; and that the definition of "false" in *Aznar v. Court of Tax Appeals*[1] (*"Aznar"*) should be revisited.

In the case at bar, the CIR found that there is falsity in McDonald's Philippines Realty Corporation ("MPRC")'s 2008 Quarterly VAT Returns. Therefore, pursuant to *Sections 203 and 222(a) of the 1997 NIRC*, he claimed that he has a period of ten (10) years to issue an assessment against MPRC. This was affirmed by the Second Division of the Court of Tax Appeals ("Court in Division") in its Decision dated October 29, 2014 and its Resolution dated February 20, 2015, wherein it defined "false" as any "deviation from the truth, whether intentional or not," pursuant to *Aznar*. Hence, the Court in Division never made a determination as to whether the falsity is intentional, it merely based the application of the ten (10) year period on the substantial under declaration by 69.86% of MPRC's gross receipts. The present draft Decision denied the two (2) Petitions for Review and affirmed the Court in Division's Decision dated October 29, 2014 and Resolution dated February 20, 2015.

I courteously disagree.

The case should be remanded to the Court in Division for the determination of intent to mislead or deceive, or of culpable negligence, on the part of MPRC.

Sections 203 and 222(a) of the 1997 NIRC mandates that the CIR should issue an assessment for deficiency taxes within three (3) years from the last day prescribed by law to file the tax return or the actual date of filing of such return, whichever comes later; and any assessment notice issued beyond this three (3)-year prescriptive period shall not be valid; save in cases wherein *e.g.* a false return was filed, assessment may be made within ten (10) years from discovery of falsity, to wit:

> SECTION 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

[1] G.R. No. L-20569, August 23, 1974, 58 SCRA 519.

> 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.
>
> xxx xxx xxx
>
> SECTION 222. *Exceptions as to Period of Limitation of Assessment and Collection of Taxes.* —
>
> (a) In the case of a false or fraudulent return with intent to evade tax or of failure to file a return, the tax may be assessed, or a proceeding in court for the collection of such tax may be filed without assessment, at any time within ten (10) years after the discovery of the falsity, fraud or omission: Provided, That in a fraud assessment which has become final and executory, the fact of fraud shall be judicially taken cognizance of in the civil or criminal action for the collection thereof.[2]

However, in order to warrant a ten (10)-year period to assess, the CIR must *(1)* not only clearly state his basis, he must also present substantial evidence in support thereto,[3] and *(2)* prove that there is an intention to mislead or deceive on the part of the taxpayer, or at least that there is culpable negligence.[4]

As I have said in the case of *Ocean Star Realty, Inc. v. Commissioner of Internal Revenue, CTA Case No. 7123, July 18, 2007,* a false return must be intentional, consisting of deception willfully and deliberately done or resorted to, *viz.*:

> False or fraudulent return, as exceptions to the period of limitation of assessment and collection of taxes provided in Section 222 of the NIRC of 1997, as amended, must be actual not constructive. It must be intentional, consisting of deception willfully and deliberately done or resorted to. Fraud must be proven by clear and convincing evidence amounting

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[2] Underscoring ours.
[3] *Commissioner of Internal Revenue v. Next Mobile, Inc.*, G.R. No. 212825, December 5, 2015, affirming the CTA's findings in *Next Mobile, Inc. v. Commissioner of Internal Revenue,* CTA Case No. 7965, December 11, 2012.
[4] *Ocean Star Realty, Inc. v. Commissioner of Internal Revenue,* CTA Case No. 7123, July 18, 2007.

> to more than mere preponderance. It cannot be justified by mere speculation. This is because fraud is never lightly to be presumed. In order to render a return made by a taxpayer a "false return" within the meaning of Section 222 of the NIRC, there must appear a design to mislead or deceive on the part of the taxpayer, or at least culpable negligence. A mistake that is not culpable in respect of its value would not constitute a false return.[5]

Likewise, below is my statement on this matter in the case of *ESS Manufacturing Company, Inc. v. Commissioner of Internal Revenue, CTA Case No. 7958, February 14, 2014:*

> In the case of *Aznar v. Court of Appeals,* the Supreme Court explained that it is quite easy for revenue officers to claim that there was falsity in the return filed by the taxpayer. However, the Court also cautioned that mere falsity of a return does not merit the application of the 10-year prescriptive period, unless it can be shown that the return was made with a design to mislead or deceive on the part of the taxpayer, or at the very least show culpable negligence.
>
> To note, the rules on prescription are put in place as a way to balance the power of the government's right to assess taxes and to protect the taxpayer from harassment by not indefinitely extending the period of assessment.
>
> In this case, respondent merely relied on the tax returns, as well as the financial statements and trial balance to substantiate her claim that the returns submitted were false; however, the same failed to show such a conclusion, and this is not enough to merit the application of the ten (10)-year period. Such falsity must be established by clear and sufficient evidence.
>
> Thus, the prescriptive period to be applied in the present case is three (3) years, as stated in Section 203 of the 1997 NIRC, as amended.[6]

In view of the above, I propose to provide the following two (2) requisites for a return to be considered false: *(1)* intention to mislead or deceive, OR culpable negligence, on the part of the taxpayer; and *(2)* substantial evidence in support thereof.

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[5] Underscoring ours.
[6] Underscoring ours.

In the case at bar, there was no finding of culpable negligence or any intent to mislead or deceive. Hence, I recommend that the case be remanded to the Court in Division as to the existence of MPRC's intent to mislead or deceive, or culpable negligence.

Should there be a finding of intent to mislead or deceive, or of culpable negligence, on the part of MPRC, only the VAT pertaining to the fourth quarter of 2008 has not prescribed.

In any case, should the Court in Division find that there is no intent to mislead or deceive or culpable negligence, the general rule of three (3) years under *Section 203 of the 1997 NIRC* applies.

Considering that the basis for the running of the three (3) year period to assess depends on the actual date of filing thereof, *Section 114(A) of the 1997 NIRC* states that the filing of the Quarterly VAT Returns must be made within twenty-five (25) days after the close of each taxable quarter, as follows:

> SECTION 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/her/its] gross sales or receipts within twenty-five (25) days following the close of each taxable quarter prescribed for each taxpayer: Provided, however, That VAT-registered persons shall pay the value-added tax on a monthly basis.[7]

Therefore, in view of MPRC's receipt of the assessment on November 22, 2011, the CIR's right to assess the first to third quarters of 2008 has prescribed and only the fourth quarter remains, to wit:

2010	DUE DATE FOR FILING OF RETURN	ACTUAL DATE OF FILING OF RETURN	BASIS	LAST DAY TO ASSESS
First Quarter	25-Apr-08	11-Apr-08	25-Apr-08	25-Apr-11
Second Quarter	25-Jul-08	21-Jul-08	25-Jul-08	25-Jul-11
Third Quarter	25-Oct-08	20-Oct-08	25-Oct-08	25-Oct-11

[7] Underscoring ours.

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Fourth Quarter	25-Jan-09	21-Jan-09	25-Jan-09	**25-Jan-12**

Having said the foregoing, I vote to **PARTIALLY GRANT** both Petitions for Review; to **REVERSE** and **SET ASIDE** the October 29, 2014 Decision and the February 20, 2015 Resolution of the Second Division of the Court of Tax Appeals; and to **REMAND** the case to the Court in Division for the proper determination of MGPRC's intent to mislead or deceive, or of culpable negligence; and correct amount of tax liability.

LOVELL R. BAUTISTA
Associate Justice

REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

EN BANC
****

MCDONALD'S PHILIPPINES REALTY CORPORATION,
Petitioner,

- versus -

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

CTA EB No. 1283
(CTA Case No. 8506)

x - x

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

- versus -

MCDONALD'S PHILIPPINES REALTY CORPORATION,
Respondent.

CTA EB No. 1284
(CTA Case No. 8506)

Present:
DEL ROSARIO, *P.J.*,
CASTAÑEDA, JR.,
BAUTISTA,
UY,
CASANOVA,
FABON-VICTORINO,
MINDARO-GRULLA,
RINGPIS-LIBAN, and
MANAHAN, *JJ.*

Promulgated:
FEB 09 2017 3:25 p.m.

x - x

CONCURRING AND DISSENTING OPINION

UY, J.:

With all due respect with the learned ponente and my other colleagues, while I concur on the ruling that McDonald's Philippines Realty Corporation is liable for value-added tax (VAT), plus the corresponding 25% surcharge imposed thereon, for calendar year

2008, as decreed by the Second Division of this Court, I dissent on the imposition of the deficiency interest thereon on the basis of Section 249(B) of the National Internal Revenue Code (NIRC) of 1997, and the inclusion of said deficiency interest in the computation of delinquency interest under Section 249(C) of the same Code.

Section 249 of the NIRC of 1997 reads:

> "SEC. 249. *Interest.* –
>
> (A) *In General.* – There shall be assessed and collected on any unpaid amount of tax, interest at the rate of twenty percent (20%) *per annum,* or such higher rate as may be prescribed by the rules and regulations, from the date prescribed for its payment until the amount is fully paid.
>
> (B) *Deficiency Interest.* – Any **deficiency** in the tax due, **as the term is defined in this Code**, shall be subject to the interest prescribed in Subsection (A) hereof, which interest shall be assessed and collected from the date prescribed for its payment until the full payment thereof.
>
> (C) *Delinquency Interest.* – In case of failure to pay:
>
> xxx xxx xxx
>
> (3) A deficiency tax, or any surcharge or interest thereon on the due date appearing in the notice and demand of the Commissioner, there shall be assessed and collected on the unpaid amount, interest at the rate prescribed in Subsection (A) hereof until the amount is fully paid, which interest shall form part of the tax." *(Emphases supplied)*

Based on the foregoing Section 249(B), the *"Deficiency Interest"* shall be imposed on "[a]*ny deficiency in the tax due, as the term is defined in this Code"*, *i.e.*, as the term "deficiency" is defined in the NIRC of 1997. Relative thereto, an examination of the said Code discloses that there are only three (3) instances where it defines the term "deficiency", and this relates only and respectively to three (3) types of internal revenue taxes, namely, income tax, estate tax, and donor's tax, pursuant to Sections 56(B), 93 and 104 of the NIRC of 1997, viz:

"SEC. 56. *Payment and Assessment of Income Tax for Individuals and Corporations.—*

xxx xxx xxx

(B) *Assessment and Payment of Deficiency Tax.—* After the return is filed, the Commissioner shall examine its and assess the correct amount of the tax. The tax or deficiency income tax so discovered shall be paid upon notice and demand from the Commissioner.

As used in this Chapter[1], in respect of a tax imposed by this Title[2], the term **'deficiency'** means:

(1) The amount by which the tax imposed by this Title exceeds the amount shown as the tax by the taxpayer upon his return; but the amount so shown on the return shall be increased by the amounts previously assessed (or collected without assessment) as a deficiency, and decreased by the amount previously abated, credited, returned or otherwise repaid in respect of such tax; or

(2) If no amount is shown as the tax by the taxpayer upon his return, or if no return is made by the taxpayer, then the amount by which the tax exceeds the amounts previously assessed (or collected without assessment) as a deficiency; but such amounts previously assessed or collected without assessment shall first be decreased by the amounts previously abated, credited, returned or otherwise repaid in respect of such tax." *(Emphasis supplied)*

"SEC. 93. *Definition of Deficiency.* — As used in this Chapter[3], the term **'deficiency'** means:

(a) The amount by which the tax imposed by this Chapter exceeds the amount shown as the tax by the executor, administrator or any of the heirs upon his return; but the amount so shown on the return shall first be increased by the amounts previously assessed (or collected without assessment) as a deficiency and

[1] Chapter IX – RETURNS AND PAYMENT OF TAX.
[2] Title II – TAX ON INCOME.
[3] CHAPTER I – ESTATE TAX (under TITLE III – ESTATE AND DONOR'S TAXES).

> decreased by the amounts previously abated, refunded or otherwise repaid in respect of such tax; or
>
> (b) If no amount is shown as the tax by the executor, administrator or any of the heirs upon his return, or if no return is made by the executor, administrator, or any heir, then the amount by which the tax exceeds the amounts previously assessed (or collected without assessment) as a deficiency; but such amounts previously assessed or collected without assessment shall first be decreased by the amounts previously abated, credited, returned or otherwise repaid in respect of such tax." *(Emphasis supplied)*
>
> "SEC. 104. *Definitions.* — xxx
>
> The term **'deficiency'** means: (a) the amount by which the tax imposed by this Chapter[4] exceeds the amount shown as the tax by the donor upon his return; but the amount so shown on the return shall first be increased by the amounts previously assessed (or collected without assessment) as a deficiency, and decreased by the amounts previously abated, refunded or otherwise repaid in respect of such tax, or (b) if no amount is shown as the tax by the donor upon his return, then the amount by which the tax exceeds the amounts previously assessed (or collected without assessment) as a deficiency, but such amounts previously assessed or collected without assessment shall first be decreased by the amounts previously abated, credited, returned or otherwise repaid in respect of such tax." *(Emphasis supplied)*

Such being the case, the deficiency interest under Section 249(B) should be applied only whenever there is a deficiency income tax, a deficiency estate tax, and a deficiency donor's tax. For this reason, in this case, no deficiency interest under Section 249(B) should be imposed on the deficiency VAT against McDonald's Philippines Realty Corporation. Correspondingly, the computation of the delinquency interest imposed under Section 249(C) should not as well include the said deficiency interest.

Correspondingly, I vote for the DELETION of: (1) the imposition

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[4] CHAPTER II – DONOR'S TAX (under TITLE III – ESTATE AND DONOR'S TAXES).

of deficiency interest on McDonald's Philippines Realty Corporation's basic deficiency VAT in the amount of ₱2,958,405.41 at the rate of 20% *per annum*; and (2) the inclusion of said deficiency interest in the computation of the delinquency interest to be imposed on the same basic deficiency VAT.

ERLINDA P. UY
Associate Justice

REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

EN BANC

MCDONALD'S PHILIPPINES REALTY CORPORATION, *Petitioner,*	**CTA *EB* NO. 1283** (CTA Case No. 8506)
-versus-	
COMMISSIONER OF INTERNAL REVENUE, *Respondent.*	

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

COMMISSIONER OF INTERNAL REVENUE, *Petitioner,*	**CTA *EB* NO. 1284** (CTA Case No. 8506)
	Present:
-versus-	**DEL ROSARIO,** *P.J.,* **CASTAÑEDA, JR., BAUTISTA, UY, CASANOVA, FABON-VICTORINO, MINDARO-GRULLA, RINGPIS-LIBAN,** *and* **MANAHAN,** *JJ.*
MCDONALD'S PHILIPPINES REALTY CORPORATION, *Respondent.*	Promulgated: FEB 09 2017 3:25 p.m.

x- -x

Dissenting Opinion

MANAHAN, J.:

With due respect to the *ponencia*, I register my dissent to the conclusions of the Court *En Banc*.

The *ponencia* applied the Supreme Court decision in *Aznar v. Court of Tax Appeals*[1] (*Aznar*), which declared that a

[1] G.R. No. L-20569, August 23, 1974, 58 SCRA 519.

return is false as long as there is a deviation from the truth, whether intentional or not. In the instant case, the Court *En Banc* agreed with the CTA Division that there was falsity in McDonalds's Philippines Realty Corporation (MPRC)'s 2008 Quarterly VAT Returns for not declaring substantial receipts from its interest income in the amount of Php24,653,378.41. Thereby, justifying the application of the ten-year prescriptive period.

However, it is my position that the applicability of the ten-year period does not apply to every "false" return and that the definition of a "false" return should be revisited in light of *Commissioner of Internal Revenue v. B.F. Goodrich Phils. Inc.*[2] (*Goodrich*), as I will discuss below.[3]

In *Aznar*, the taxpayer was assessed with deficiency income tax for six consecutive taxable years due to his gross under-declaration of taxable income. These substantial under-declarations were noted by the Supreme Court and were made the indicia of the falsity of income tax returns. The Court went on to state that the "very substantial under-declarations of income for six consecutive years eloquently demonstrate the falsity or fraudulence of the income tax returns with an intent to evade the payment of tax. Furthermore, the Court expounded on the concept of false returns as being distinct from fraudulent returns with intent to evade taxes, as follows:

> We believe that the proper and reasonable interpretation of said provision should be that in the three different cases of (1) false return, (2) fraudulent return with intent to evade tax, (3) failure to file a return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within ten years after the discovery of the (1) falsity, (2) fraud, (3) omission. Our stand that the law should be interpreted to mean a separation of the three different situations of false return, fraudulent return with intent to evade tax, and failure to file a return is strengthened immeasurably by the last portion of the provision which segregates the situations into three different classes, namely – 'falsity,' 'fraud[,]' and 'omission.' That there is a difference between 'false return' and 'fraudulent return' cannot be denied. While the first merely implies deviation from the truth, whether intentional or not, the second implies

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[2] G.R. No. 104171, February 24, 1999, 303 SCRA 546.
[3] Part of the discussion is based on my article: *False Returns*, 55 Ateneo Law Journal 354, September 2010.

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> intentional or deceitful entry with intent to evade the taxes due.[4]

Based on this decision, the Court has categorized wrongful entries, intentional or unintentional, or mistakes made, whether in good faith or in bad faith, appearing on the face of tax returns, as "falsity" which constitutes a legal ground for the imposition of the ten-year period of prescription.

Almost 25 years later, the Supreme Court promulgated its *Goodrich* decision, which shows a softening of the Court's stance on the scope and coverage of "false return" as compared to the position in *Aznar.*

In *Goodrich,* the taxpayer sold a piece of real property at a price which was lower than its declared fair market value. The Bureau of Internal Revenue (BIR) insisted that "falsity" was committed thereby justifying the issuance of the assessment beyond the normal three-year prescriptive period. In finding that the assessment had prescribed, the Supreme Court commented on the issue of falsity, as follows:

> Petitioner insists that private respondent committed "falsity" when it sold the property for a price lesser than its declared fair market value. <u>This fact alone did not constitute a false return which contains wrong information due to mistake, carelessness or ignorance</u>. It is possible that real property may be sold for less than adequate consideration for a *bona fide* business purpose; in such event, the sale remains an "arm's length" transaction. In the present case, the private respondent was compelled to sell the property even at a price less than its market value, because it would have lost all ownership rights over it upon the expiration of the parity amendment. Xxx
>
> Furthermore, <u>the fact that private respondent sold its real property for a price less than its declared fair market value did not by itself justify a finding of false return</u>. Indeed, private respondent declared the sale in its 1974 return submitted to the BIR. Within the five-year prescriptive period [now, three-year prescriptive period], the BIR could have issued the questioned assessment, because the declared fair market value of the said property was of public record. This it did not do,

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[4] G.R. No. L-20569, August 23, 1974, 58 SCRA 519 (underscoring supplied).

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> however, during all those five years. Moreover, the BIR failed to prove that respondent's 1974 return had been filed fraudulently. Equally significant was its failure to prove respondent's intent to evade the payment of the correct amount of tax.[5]

While *Aznar* and *Goodrich* have radically different factual milieus, both these cases impacted on how "false returns" are defined. From the broad *Aznar* definition that a false return is any deviation from the truth, *Goodrich* provided an instance wherein a "deviation" from the truth as found by the BIR, did not automatically render the return as a "false return" which would justify the application of the ten-year prescriptive period.

Furthermore, in *Goodrich*, the Supreme Court required that the BIR prove the presence of fraudulent intent or intent to evade payment of the correct amount of tax on the part of the taxpayer. The Supreme Court also found that the BIR could have issued the assessment within the ordinary prescriptive period considering that the declared fair market value was in the public record. In *Goodrich*, the "deviation" did not put the BIR at a disadvantage in issuing its assessment, as opposed to the situation in *Aznar* which involved exorbitant under-declarations for six consecutive years which could not have been easily traced from the returns itself.

This is consistent with the statement in *Aznar*:

> The ordinary period of prescription of 5 years within which to assess tax liabilities under Sec. 331 of the NIRC should be applicable in normal circumstances, but <u>whenever the government is placed at a disadvantage so as to prevent its lawful agents from proper assessment of tax liabilities due to false returns, fraudulent return intended to evade payment of tax or failure to file returns, the period of ten years ...from the time of the discovery of the falsity, fraud or omission...should be the one enforced</u>.[6]

Thus, as early as *Aznar*, a qualification had been made that there should be a disadvantage to the government agents resulting from falsity, fraud or omission, which would prevent said agents from assessing the tax within the ordinary period

[5] G.R. No. 104171, February 24, 1999, 303 SCRA 546 (underscoring supplied).
[6] G.R. No. L-20569, August 23, 1974, 58 SCRA 519 (underscoring supplied).

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of prescription. Without such disadvantage, the normal three-year prescriptive period should apply.

It is perhaps interesting to note that even prior to *Goodrich,* the CTA, in 1995, had also recognized this limitation in *Aznar,* to wit:

> Respondent also contends in the alternative, that petitioner's omission of its sales of bottled and tetra-packed milk from its sales tax return rendered said returns "false" within the meaning of Section 223 of the Tax Code. In support of this, reliance is placed on the ruling in the case of Aznar vs. Court of Tax Appeals (58 SCRA 519), wherein it was held that the term "false return" merely implied a deviation from truth, irrespective of whether such omission is intentional or not. Thus, respondent argues, since petitioner's sales tax returns did not disclose the "truth" regarding its sales of bottled and tetra-packed milk to outlets other than the Armed Forces of the Philippines Commissary and Exchange Service (AFPCES) and the US Military Installations (USMI), such omission rendered said returns "false" within the contemplation of Section 223 of the Tax Code.
>
> We find respondent's reliance on Aznar misplaced. <u>There is nothing in the said case which establishes a hard and fast rule that every "deviation" from the truth necessarily brings a particular return under the coverage of Section 223 of the Tax Code</u>. As pointed out by the petitioner, <u>it is only where the falsity or "deviation" would place the government at a disadvantage so as to prevent the assessment and collection of the correct amount of taxes that the ordinary prescriptive period ...should not be applied</u>.[7]

Finally, it is necessary to apply the *Aznar* and *Goodrich* doctrines in light of the purpose and rationale for providing a prescriptive period.

> It must be kept in mind that the very reason why the law provided for prescription is to give taxpayers peace of mind, that is, to safeguard them from unreasonable examination, investigation, or assessment. <u>The law on prescription, being a remedial measure,</u>

[7] San Miguel Corporation v. Commissioner of Internal Revenue, CTA Case No. 4675, January 6, 1995 (underscoring supplied).

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> should be liberally construed in order to afford such protection. As a corollary, the exceptions to the law on prescription should perforce be strictly construed.[8]

Guided by the foregoing, the application of *Aznar* should not be one of unbridled discretion.[9] This is especially true considering that taxes are self-assessed, as discussed by the Supreme Court:

> Taxes are generally self-assessed. They are initially computed and voluntarily paid by the taxpayer. The government does not have to demand it. If the tax payments are correct, the BIR need not make an assessment.
>
> The self-assessing and voluntarily paying taxpayer, however, may later find that he or she has erroneously paid taxes.[10]

Upon finding that a tax has been paid erroneously, the taxpayer is allowed to file a claim for refund. On the reverse side, should the taxpayer find that there is an error in its return, the taxpayer may file an amended return, or should the BIR be the one to detect the error, then an assessment shall be issued.

The very meaning of a deficiency assessment is that there was an error or omission on the part of the taxpayer in the preparation of its return or the payment of its tax. But each and every error, as discussed previously, does not and should not result to the operation of the ten-year prescriptive period. Otherwise, on the strength of the *Aznar* doctrine, BIR examiners conducting regular tax audits, who, logically as a matter of course, would always come up with tax findings of either under-declaration of income or over-declaration of deductions, or both, could mercilessly and arbitrarily raise the argument of false return giving rise to the ten-year prescriptive period. The result would be a lackadaisical implementation of the statutory principle that the statute of limitations is a remedial measure and should be strictly construed against the taxing authority and liberally in favor of the taxpayer.

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[8] Commissioner of Internal Revenue v. Standard Chartered Bank, G.R. No. 192173, July 29, 2015, citing CIR v. B.F. Goodrich Phils, Inc.

[9] Ayala Hotels, Inc. v. Commissioner of Internal Revenue, CTA Case No. 6002, January 10, 2002.

[10] SMI-ED Phils. Techonology, Inc. v. Commissioner of Internal Revenue, G.R. No. 175410, November 12, 2014.

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It is unfortunate that the case of *Commissioner of Internal Revenue v. Ayala Hotels, Inc.*[11] (*Ayala*), cited by MPRC, was not ruled upon by the Supreme Court due to the failure of therein petitioner to file its petition for review on certiorari. However, the Court of Appeals' discussion aptly described the effect of a sweeping application of *Aznar*, as quoted below:

> Reliance on the *Aznar Case* with regard to the issue of prescription is misplaced. Although in the said case, the Supreme Court ruled that a "false return" merely implies a deviation from the truth, whether intentional or not, such pronouncement should not be given a sweeping application in all cases where a mistake in ITR entries are made by taxpayers. Otherwise, any mistake, however slight, in a return filed by a taxpayer in good faith would justify the application of the ten-year prescriptive period for assessment. Consequently, the protection provided for under Section 203 of the 1997 NIRC is rendered nugatory. Logically therefore, not all "false returns" would call for an application of Section 222 of the 1997 NIRC. Only "false returns" which are filed by a taxpayer with intent to evade tax should warrant an application of the ten-year prescriptive period.
>
> In order to render a return made by a taxpayer a "false return" within the meaning of Section 222, of the Tax Code, there must appear, a design to mislead or deceive on the part of the taxpayer, or at least culpable negligence. A mistake, not culpable in respect of its value would not constitute a false return.[12]

Notwithstanding, there is sufficient basis provided by *Aznar* and *Goodrich* to limit the application of the ten-year period to certain factual circumstances.

Thus, in the instant case (1) there was no design to mislead or deceive on the part of MPRC since it had acted in good faith and under an honest belief that its interest income was not incurred in the course of trade or business nor incidental to its leasing business on the basis of previous interpretations of government agencies and jurisprudence;[13] (2) the alleged deviation was not an intentional mistake or omission so as to put the BIR at a disadvantage in the

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[11] G.R. No. 163595, April 11, 2005; CA-G.R. SP No. 70025, April 19, 2004.
[12] CA-G.R. SP No. 70025, April 19, 2004 (underscoring supplied).
[13] Decision dated October 29, 2014, *rollo*, p. 67; Petitioner's Memorandum, *rollo*, pp. 164-174.

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investigation and assessment since the BIR was not prevented from issuing an assessment on the alleged under-declaration within the three-year period considering that the subject interest income was declared in, and easily determinable from MPRC's Audited Financial Statements for the years ended December 31, 2008 and 2007, and 2008 Annual Income Tax Return[14]; and (3) there was no fraudulent intent or intent to evade the payment of the correct amount of tax. Hence, the foregoing circumstances do not justify the application of the ten-year period.

For all the foregoing, I vote to deny the Petition for Review filed by the Commissioner of Internal Revenue in CTA EB No. 1284. On the other hand, I vote to grant MPRC's Petition for Review in CTA EB No. 1283 on the ground that the assessment for deficiency Value-Added Tax (VAT) for taxable year 2008 has prescribed.

CATHERINE T. MANAHAN
Associate Justice

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[14] Decision dated October 29, 2014, *rollo*, p. 80.