A PROPOSED APPROACH TO STREAMLINE THE IMPOSITION OF INTEREST IN TAX REFUND CASES*

*Jonas Miguelito P. Cruz***

ABSTRACT

When one owes money to another, it is usual to pay interest. But when the government owes money to a taxpayer for exacting a tax it has erroneously or illegally collected, interest is generally not imposed. Jurisprudence has provided two rules on this subject: (1) that the government is not obliged to pay interest because there is no statutory provision that directs it ("No Statutory Authority Test") to do so; and (2) interest may only be imposed in case there is arbitrariness ("Arbitrariness Test"). This Note discusses the concepts of tax refunds and interest, and the prevailing laws and jurisprudence on the matter. It also shows, upon examination of the text not just of the Tax Code but all other statutes and case law on the imposition of interest, that the No Statutory Authority Test is not a proper justification to preclude the imposition of interest in tax refund cases. The Arbitrariness Test continues to be the most appropriate standard used in determining whether it is appropriate in each case to impose interest. This Note proposes a more streamlined set of guidelines on the imposition of interest using the Arbitrariness Test, considering the cardinal principle of due process of law and comparative judicial review standards for arbitrary and capricious acts.

---

* *Cite as* Jonas Miguelito C. Cruz, *A Proposed Approach to Streamline the Imposition of Interest in Tax Refund Cases,* 95 PHIL. L. J. 86, [page cited] (2022).

** J.D., University of the Philippines College of Law (2020); B.S. Business Administration & Accountancy, UP College of Business Administration (2014); Chair, Editorial Board, PHILIPPINE LAW JOURNAL Volume 91 (2017–2018). The author currently serves as Executive Assistant in the Office of Presiding Justice of the Court of Tax Appeals. The views expressed by the author in this Note are his alone and do not reflect those of the institutions he is associated with. The author would like to express his gratitude to Presiding Justice Roman G. Del Rosario and his colleagues at the Court of Tax Appeals for their invaluable support in the writing of this Note.

INTRODUCTION

"Money makes money. And the money that makes money, makes money."[1] This quote from the American founding father Benjamin Franklin encapsulates in simple terms the concept of interest, which has existed since the advent of human civilization. The ancient literature of different religions even provides for proscriptions on the imposition of unreasonably high rates called "usury."[2] Yet, interest has remained and has become the foundation of the growing modern economy. Without interest, there is no incentive for the lender to part with his or her money, and "[b]y the use of credit, more exchanges are possible, persons are able to enjoy a thing today but pay for it later, and through the banking system, actual money transfer is eliminated by the cancellation of debts and credits."[3]

It is thus usual for interest to be paid when one owes money to another. Interest is simply the "cost of borrowing money."[4] But there are certain instances when the imposition of interest is generally prohibited, not because of religious, social, or moral proscription as in the case of usury, but because the law has provided for a built-in advantage to the person or entity who owes the money. Tax refunds are a prime example.

In the Philippines, the taxing authority is generally not required to pay interest on claims for the refund of tax. Among the key reasons why interest is not generally imposed is because the government is the adverse party. It has been a developed part of legal hermeneutics that taxes are the "lifeblood" of the government, such that their "prompt and certain availability is an imperious need."[5] From the perspective of the revenue agencies, refund claims by taxpayers are like mosquitoes that suck the nutrients out of the government's bloodstream. As such, the rule that tax refunds are construed

---

[1] *See* BURTON G. MALKIEL & CHARLES D. ELLIS, THE ELEMENTS OF INVESTING: EASY LESSONS FOR EVERY INVESTOR 11 (2013).

[2] *See* Joshua Vincent, *Historical, Religious and Scholastic Prohibition of Usury: The Common Origins of Western and Islamic Financial Practices*, Law School Student Scholarship (2014), *available at* https://scholarship.shu.edu/student_scholarship/600.

[3] HECTOR S. DE LEON & HECTOR M. DE LEON, JR., COMMENTS AND CASES ON CREDIT TRANSACTIONS 1 (2016), *citing* CLIFFORD L. JAMES, PRINCIPLES OF ECONOMICS 130 (1956).

[4] Abella v. Abella [hereinafter "*Abella*"], G.R. No. 195166, 762 SCRA 221, 232, July 8, 2015.

[5] Comm'r of Internal Revenue v. Pineda, G.R. No. 22734, 21 SCRA 105, 110, Sept. 15, 1967.

strictly against the taxpayer and liberally in favor of the government has developed.[6] The prevailing law acts as a firewall against refund claims.

But why are tax refunds an exception? If the government owes money to a taxpayer where the tax was, say, erroneously or illegally collected, why is the government then precluded from paying the taxpayer the amount and the cost of the money foregone without his or her fault? Is it always the case that the government cannot be compelled to pay interest because all its acts, even the erroneous and illegal collection of tax, are presumed to be correct and done in good faith?[7] The taxpayer is thus left at a disadvantage when claiming tax refunds. As compensation to the taxpayer and as a deterrent against the taxing authority treating refund claims lightly, it is time to impose interest in tax refund cases under clear and workable guidelines.

The Supreme Court has proffered two reasons why interest is generally not imposed on refund claims. *First*, there is no statute that allows for the clear and express imposition of interest in tax refunds. The Court has ruled that there is no provision in the National Internal Revenue Code[8] that provides for payment by the Bureau of Internal Revenue (BIR) of any interest in tax refund claims. *Second*, interest is generally not imposable, except when the collection of tax was attended with "arbitrariness." Thus, if the claim for tax refund was made in good faith or if there was merely an honest difference of opinion in interpreting the tax law, there is no need to impose interest.

This Note aims to show that the current standards as formulated in jurisprudence are contradictory with each other. For if the Court is of the view that there is no provision that mandates the imposition of interest, then what is the statutory authority for the imposition of interest when there is arbitrariness? Likewise, if it is the Court's duty to harmonize the various statutes to form a "complete, coherent, and intelligible system" of law,[9] then the review and harmonization of the different provisions should not be limited to provisions within the Tax Code, but also to all other laws regarding the imposition of interest. It is the purpose of this Note to show that the current standards on the imposition of interest on tax refunds are conflicting, and to propose in their stead clear and workable guidelines.

---

[6] United Airlines, Inc. v. Comm'r of Internal Revenue, G.R. No. 178788, 631 SCRA 567, 582, Sept. 29, 2010.

[7] *See* Comm'r of Internal Revenue v. Hantex Trading Co., Inc., G.R. No. 136975, 454 SCRA 301, 329, Mar. 31, 2005.

[8] Rep. Act No. 8424 (1997).

[9] Phil. Econ. Zone Auth. v. Green Asia Constr. & Dev. Corp., G.R. No. 188866, 659 SCRA 756, 764, Oct. 19, 2011, *citing* Honasan v. Panel of Investigating Prosecutors of the DOJ, G.R. No. 159747, 427 SCRA 46, 70, Apr. 13, 2004.

Part I of this Note explains the tax refund process for both administrative and judicial claims between the two types of tax refunds. Part II discusses the concept of interest and its nature as either monetary or compensatory, and determines its applicability to tax refunds. Part III explains the current rule on the imposition of interest in tax refund cases through their statutory and jurisprudential bases. Part IV proposes a refinement of the existing rule on the imposition of interest and presents a workable set of guidelines that may be used by the courts. Finally, a conclusion is offered to synthesize the discussion in this Note. It is to be noted that the discussions herein are limited only to national internal revenue taxes; however, similar and analogous concepts may be applied to customs duties and taxes under the Customs Modernization and Tariff Act (CMTA),[10] and to local taxes under the Local Government Code,[11] which are subjects of another discussion.

I. TAX REFUND PROCESS

To fully understand the tax refund process under the Tax Code, there is a need to determine the nature of the overpayment, whether it is for the: (1) recovery of tax erroneously or illegally collected; or (2) refund or credit of input tax in the case of value-added tax (VAT). It is essential to differentiate the two because of their divergent procedural and substantive requirements.

A. Recovery of Erroneously or Illegally Collected Tax

Section 204(C) of the Tax Code provides for the procedure in filing an administrative claim for refund of erroneously or illegally collected tax, *viz.*:

> Sec. 204. *Authority of the Commissioner to Compromise, Abate and Refund or Credit Taxes.* – [. . .]
>
> * * *
>
> (C) Credit or refund taxes erroneously or illegally received or penalties imposed without authority, refund the value of internal revenue stamps when they are returned in good condition by the purchaser, and, in his discretion, redeem or change unused stamps that have been rendered unfit for use and refund their value upon proof of destruction. No credit or refund of taxes or penalties shall be allowed unless the taxpayer files in writing with the

[10] Rep. Act No. 10863 (2016).
[11] Rep. Act No. 7160 (1991).

> Commissioner a claim for credit or refund within two (2) years after the payment of the tax or penalty: *Provided, however*, That a return filed showing an overpayment shall be considered as a written claim for credit or refund.[12]

Thus, a taxpayer who is subject to tax which was erroneously or illegally collected may file a written claim for refund before the Commissioner within two years after the payment of the tax. For example, if a corporation files its income tax return for taxable year 2020 on April 15, 2021 and there was an erroneous or illegal collection of tax for the year covered; then the corporate taxpayer must file an administrative claim with the Commissioner on or before April 15, 2023, or two years after the payment of the corporate income tax.

During the two-year period, the taxpayer should be on the lookout for the decision of the Commissioner. If the latter denies the refund claim within the said period, the taxpayer has recourse to file an appeal with the Court of Tax Appeals (CTA) within 30 days from receipt of such decision.[13] However, the filing of the appeal must also be within two years after the payment of the tax, like the prescriptive period for the administrative claim, as provided under Section 229 of the Tax Code:

> Sec. 229. *Recovery of Tax Erroneously or Illegally Collected.* – No suit or proceeding shall be maintained in any court for the recovery of any national internal revenue tax hereafter alleged to have been erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority, of any sum alleged to have been excessively or in any manner wrongfully collected without authority, or of any sum alleged to have been excessively or in any manner wrongfully collected, until a claim for refund or credit has been duly filed with the Commissioner; but such suit or proceeding may be maintained, whether or not such tax, penalty, or sum has been paid under protest or duress.
>
> In any case, no such suit or proceeding shall be filed after the expiration of two (2) years from the date of payment of the tax or penalty regardless of any supervening cause that may arise after payment: *Provided, however*, That the Commissioner may, even without a written claim therefor, refund or credit any tax, where on the face of the return upon which payment was made, such payment appears clearly to have been erroneously paid.[14]

---

[12] TAX CODE, § 204(C).
[13] Rep. Act No. 1125 (1954), *amended by* Rep. Act No. 9282 (2004), § 11.
[14] TAX CODE, § 229.

Therefore, the taxpayer should be able to file both the administrative and judicial claims for refund within the same two-year period after payment of the tax. It must be noted that under Section 229 of the Tax Code, a judicial claim must always be preceded by an administrative claim. Is it then required that there should first be a decision or resolution by the Commissioner on the administrative claim before a judicial claim may be filed?

The Supreme Court has ruled in a number of cases that there is no need for the taxpayer to wait for the decision of the Commissioner on its administrative claim for refund. What the law requires is that both the administrative and judicial claims be filed within the two-year period and that the administrative claim be filed first. If the taxpayer is forced to wait for the action of the Commissioner beyond the two-year period, then he or she is forced to forfeit the right to file a judicial claim, as provided for under Section 229 of the Tax Code. In *CBK Power Co., Ltd. v. Commissioner of Internal Revenue*,[15] the Supreme Court ruled that the taxpayer is not required to wait for the decision of the Commissioner on its refund claim, holding that if the "[petitioner] awaited the action of the Commissioner on its claim for refund prior to taking court action knowing fully well that the prescriptive period was about to end, it would have lost not only its right to seek judicial recourse but its right to recover the [...] taxes it erroneously paid to the government thereby suffering irreparable damage."[16] As explained by the Court, the administrative claim is primarily intended as a "notice of warning" to the Commissioner that unless the taxpayer is refunded of the erroneously or illegally collected tax, recourse to the courts shall ensue.[17] Citing the 1953 case of *P.J. Kiener Co., Ltd. v. David*,[18] which interpreted Section 306 of the 1939 Tax Code[19] (now Section 229 of the prevailing Tax Code), the Court ruled that:

> The controversy centers on the construction of the aforementioned section of the Tax Code which reads:
>
> > SEC. 306. *Recovery of tax erroneously or illegally collected.* — No suit or proceeding shall be maintained in any court for the recovery of any national internal revenue tax hereafter alleged to have been erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority, or of any sum alleged to have been excessive or in any manner

[15] G.R. No. 193383, 746 SCRA 93, Jan. 14, 2015

[16] *Id.* at 110.

[17] *Id.*

[18] [Hereinafter "P.J. Kiener"], G.R. No. 5163, 92 Phil. 945, Apr. 22, 1953.

[19] Comm. Act No. 466 (1939).

> wrongfully collected, until a claim for refund or credit has been duly filed with the Collector of Internal Revenue; but such suit or proceeding may be maintained, whether or not such tax, penalty, or sum has been paid under protest or duress. In any case, no such suit or proceeding shall be begun after the expiration of two years from the date of payment of the tax or penalty.
>
> The preceding provisions seem at first blush conflicting. It will be noticed that, whereas the first sentence requires a claim to be filed with the Collector of Internal Revenue before any suit is commenced, the last makes imperative the bringing of such suit within two years from the date of collection. But the conflict is only apparent and the two provisions easily yield to reconciliation, which it is the office of statutory construction to effectuate, where possible, to give effect to the entire enactment.
>
> To this end, and bearing in mind that the Legislature is presumed to have understood the language it used and to have acted with full idea of what it wanted to accomplish, it is fair and reasonable to say without doing violence to the context or either of the two provisions, that by the first is meant simply that the Collector of Internal Revenue shall be given an opportunity to consider his mistake, if mistake has been committed, before he is sued, but not, as the appellant contends that pending consideration of the claim, the period of two years provided in the last clause shall be deemed interrupted. Nowhere and in no wise does the law imply that the Collector of Internal Revenue must act upon the claim, or that the taxpayer shall not go to court before he is notified of the Collector's action. [...] We understand the filing of the claim with the Collector of Internal Revenue to be intended primarily as a notice of warning that unless the tax or penalty alleged to have been collected erroneously or illegally is refunded, court action will follow.[20]

Thus, as the Supreme Court held in the recent case of *Commissioner of Internal Revenue v. Univation Motor Philippines, Inc.*,[21] the filing of the judicial claim, sans action by the Commissioner on the administrative claim, does not run afoul of the doctrine of exhaustion of administrative remedies,[22] precisely

---

[20] *P.J. Kiener*, 92 Phil. at 946–47.

[21] G.R. No. 231581, 901 SCRA 512, 521-22, Apr. 10, 2019.

[22] *See* Power Sector Assets and Liab. Mgmt. Corp. v. Comm'r of Internal Revenue, G.R. No. 198146, 835 SCRA 235, 266, Aug. 8, 2017. "[U]nder the doctrine of exhaustion of administrative remedies, it is mandated that where a remedy before an administrative body is provided by statute, relief must be sought by exhausting this remedy prior to bringing an action

because the law only mandates that a prior claim before the Commissioner must have been filed. The purpose of the administrative claim is merely to give the Commissioner an opportunity to act on the taxpayer's refund request, and the taxpayer is not bound to wait for the Commissioner's decision.

It is also well to remember that the reckoning point in filing both the administrative and judicial claims for refund is from the time the tax was paid.[23] However, while the law provides that the two-year period is counted from the date of payment of the tax, jurisprudence provides that the two-year prescriptive period to claim a refund actually commences to run, at the earliest, on the date of the filing of the final adjustment return or the annual income tax return, when it can be finally ascertained if the taxpayer still has to pay additional income tax or if he or she is entitled to a refund of overpaid income tax.[24]

B. Refunds or Tax Credits of Input Tax

With regard to VAT, the Tax Code provides for a different procedure in claiming excess and unutilized input tax. VAT is a form of business tax imposed on a person, engaged in the course of trade or business, who sells barters, exchanges, leases goods or properties, renders services, and imports goods.[25] When a VAT-registered entity buys goods from a local VAT-registered seller, input tax is incurred, and when such VAT-registered entity sells goods, there is output tax. The VAT payable of the VAT-registered entity is the difference between its output tax and input tax. However, when there is excess input tax, the taxpayer may use such input tax in the succeeding taxable quarters or apply for a refund of such input tax. Refund of input tax is allowed when a VAT-registered entity has zero-rated or effectively zero-rated sales of goods or services,[26] or when the output tax is subjected to 0% VAT. This is usual for companies that export goods to buyers abroad in exchange for acceptable foreign currency,[27] render certain kinds of services to non-resident foreign corporations doing business outside the Philippines,[28] or

---

in court in order to give the administrative body every opportunity to decide a matter that comes within its jurisdiction."

[23] Comm'r of Internal Revenue v. Manila Electric Co. [Hereinafter "*MERALCO*"], G.R. No. 181459, 725 SCRA 384, 398, June 9, 2014.

[24] ACCRA Investments Corp. v. Ct. of Appeals, G.R. No. 96322, 204 SCRA 957, 964, Dec. 20, 1991.

[25] TAX CODE, § 105.

[26] § 110(B).

[27] § 106(A)(2).

[28] § 108(B).

sell goods to entities located in special economic zones (ecozones) in the country under the so-called "Cross Border Doctrine."[29]

Sections 112(A) and (C) provide for the procedure to file refund claims of excess and unutilized input tax, as follows:

> Sec. 112. *Refunds or Tax Credits of Input Tax.* –
>
> (A) *Zero-rated or Effectively Zero-rated Sales.* - Any VAT-registered person, whose sales are zero-rated or effectively zero-rated may, within two (2) years after the close of the taxable quarter when the sales were made, apply for the issuance of a tax credit certificate or refund of creditable input tax due or paid attributable to such sales, except transitional input tax, to the extent that such input tax has not been applied against output tax: *Provided, however*, That in the case of zero-rated sales under Section 106(A)(2)(a)(1), (2) and (b) and Section 108 (B)(1) and (2), the acceptable foreign currency exchange proceeds thereof had been duly accounted for in accordance with the rules and regulations of the *Bangko Sentral ng Pilipinas* (BSP): *Provided, further*, That where the taxpayer is engaged in zero-rated or effectively zero-rated sale and also in taxable or exempt sale of goods of properties or services, and the amount of creditable input tax due or paid cannot be directly and entirely attributed to any one of the transactions, it shall be allocated proportionately on the basis of the volume of sales. *Provided, finally*, That for a person making sales that are zero-rated under Section 108(B)(6), the input taxes shall be allocated ratably between his zero-rated and non-zero-rated sales.
>
> * * *
>
> (C) *Period within which Refund of Input Taxes shall be Made.* - In proper cases, the Commissioner shall grant a refund for creditable input taxes within ninety (90) days from the date of submission of the official receipts or invoices and other documents in support of the application filed in accordance with Subsections (A) and (B) hereof: *Provided*, That should the Commissioner find that the grant of refund is not proper, the Commissioner must state in writing the legal and factual basis for the denial.

---

[29] *See* Coral Bay Nickel Corp. v. Comm'r of Internal Revenue, G.R. No. 190506, 793 SCRA 190, 198, June 13, 2016. "The provision thereby establishes the fiction that an ECOZONE is a foreign territory separate and distinct from the customs territory. Accordingly, the sales made by suppliers from a customs territory to a purchaser located within an ECOZONE will be considered as exportations."

> In case of full or partial denial of the claim for tax refund, the taxpayer affected may, within thirty (30) days from the receipt of the decision denying the claim, appeal the decision with the Court of Tax Appeals: *Provided, however*, That failure on the part of any official, agent, or employee of the BIR to act on the application within ninety (90) days period shall be punishable under Section 269 of this Code.

Prior to the enactment of the Tax Reform for Acceleration and Inclusion Law (TRAIN),[30] the period within which the Commissioner must decide a refund claim of excess and unutilized input VAT was 120 days. However, TRAIN shortened the period to 90 days. The recently enacted Corporate Recovery and Tax Incentives for Enterprises Act (CREATE)[31] likewise imposed a 90-day period for the Commissioner to decide on refund claims of erroneously or illegally collected taxes, but this provision was vetoed by the President. TRAIN also removed from the said provision any mention of tax credit certificates as an alternative that the Commissioner may issue to the taxpayer, instead of an actual cash refund.[32] Likewise, TRAIN removed from Section 112(C) the phrase "or the failure on the part of the Commissioner to act on the application within the period prescribed above" as one of the grounds for appeal to the CTA. However, even with this deletion it is believed that the taxpayer still has recourse to file an appeal because the jurisdiction of the CTA, under its charter, specifically includes "[i]naction by the Commissioner of Internal Revenue in cases involving [...] refunds of internal revenue taxes, fees or other charges, penalties in relations thereto, [...] where the National Internal Revenue Code ['NIRC'] provides a specific period of action, in which case the inaction shall be deemed a denial."[33] Even if the present Tax Code does not expressly provide that the failure of the Commissioner to act on the refund claim within the 90-day period is appealable to the CTA, the law creating the CTA, which was not expressly repealed by TRAIN,[34] still vests with the said Court subject matter

---

[30] Rep. Act No. 10963 (2017).

[31] Rep. Act No. 11534 (2021), § 14.

[32] S. Journal 535, 17th Cong., 2nd Sess. (Oct. 3, 2017). "Asked on the rationale for the deletion of the phrase 'tax clearance certificates' in Section 24 which amended Section 112 of the Tax Code, thus giving the government the option to pay through tax clearance certificates instead of cash, Senator Angara recalled that the concept of a tax credit certificate was created at the start of the imposition of the VAT in the 1980s when the Philippines did not have enough cash to pay the refunds. He explained that while tax credit certificates became a cash management tool at the time, the bill seeks to bring back refunds to its true form as cash refunds so that the Philippines could be at par with international standards."

[33] Rep. Act No. 1125 (1954), *amended by* Rep. Act No. 9282 (2004), §§ 7(a)(2), 11. *See also* A.M. No. 05-11-07-CTA (2005), rule 4, § 3(a)(2), *and* rule 8, § 3(a). Revised Rules of the Court of Tax Appeals.

[34] Rep. Act No. 10963 (2017), § 86.

jurisdiction[35] over the inaction of the Commissioner.[36] If Congress intended to remove the inaction by the Commissioner from the CTA's jurisdiction, then such intent could have been clearly expressed by repeal or amendment of the CTA charter. Assuming that an implied repeal exists, the more appropriate course is to give full effect to the view that the Tax Court retains jurisdiction over inaction by the Commissioner, there being no irreconcilable conflict between the Tax Code and the CTA charter.

The law provides for a different procedure in the refund claims of excess and unutilized input taxes primarily because these taxes are not considered taxes erroneously or illegally collected. As held in the case of *Coca-Cola Bottlers Philippines, Inc. v. Commissioner of Internal Revenue*,[37] "[t]he term 'excess' input VAT simply means that the input VAT available as credit exceeds the output VAT, not that the input VAT is excessively collected because it is more than what is legally due."[38] Hence, Sections 204(C) and 229 of the Tax Code are inapplicable when the issue is the determination of whether the taxpayer is entitled to a refund of excess and unutilized input tax.[39]

Thus, the general rule in claiming excess and unutilized input tax is that the administrative claim for refund should be filed within two years after the close of the taxable quarter when the sales were made. For example, if the refund claim covers the first quarter of calendar year 2020, then the refund claim should be filed not later than March 31, 2022. Thereafter, the Commissioner shall decide within 90 days (previously 120 days) from the submission of the official receipts, invoices, and other supporting documents. If the Commissioner denies the claim, wholly or partially, the factual and legal

---

[35] *See* Mitsubishi Motors Phils. Corp. v. Bureau of Customs, G.R. No. 209830, 759 SCRA 306, 312, June 17, 2015. "It is axiomatic that jurisdiction over the subject matter is the power to hear and determine the general class to which the proceedings in question belong; it is conferred by law and not by the consent or acquiescence of any or all of the parties or by erroneous belief of the court that it exists."

[36] Though there is no jurisprudence yet interpreting the deletion of "inaction" as one of the grounds for filing an appeal with the CTA under Section 112(C) of the Tax Code, such deletion did not in any way remove the jurisdiction of the CTA per Section 7(a)(2) of Rep. Act No. 1125 (1957), as amended by Rep. Act No. 9282 (2004), to decide cases where there is inaction on the part of the Commissioner. In the author's view, the 90-day period remains to be mandatory and jurisdictional on the part of the taxpayer in filing his or her judicial claim for refund. *See* Alvin R. Tan, Jonas Miguelito P. Cruz & Tanya Renee F. Rosales, *"Deemed Denied" is Still Alive: Why the Court of Tax Appeals Continues to Exercise Jurisdiction over Inactions on Refund Claims of Input Tax*, 65 ATENEO L.J. 1081 (2021).

[37] G.R. No. 222428, 856 SCRA 64, Feb. 19, 2018

[38] *Id.* at 72-73.

[39] Comm'r of Internal Revenue v. Aichi Forging Co. of Asia, Inc. [hereinafter "*Aichi*"], G.R. No. 184823, 632 SCRA 422, 438, Oct. 6, 2010.

bases therefor should be stated in writing, and the taxpayer may file an appeal before the CTA within 30 days from receipt of the decision. If there is inaction on the part of the Commissioner to decide on the claim within the 90-day period, the taxpayer may also file an appeal before the CTA within 30 days from the lapse of the 90-day period. Thus, the taxpayer must wait for the Commissioner to decide during the 90-day period since an appeal filed during such time is premature; but upon the lapse of the 90-day period, the inaction is "deemed a denial" of the refund application, over which the CTA has jurisdiction.[40]

In recent years, the Supreme Court has rendered decisions that have clarified the various issues surrounding refunds of excess and unutilized input tax. One of these seminal decisions is *San Roque Power Co. v. Commissioner of Internal Revenue*[41] where the Court, sitting *en banc*, ruled that the "120+30" (now "90+30") day period is mandatory and jurisdictional on the part of the taxpayer claiming a refund of excess and unutilized input tax, and that the two-year period to file an administrative claim must likewise be observed. However, in harmonizing the various jurisprudence on the matter,[42] and the BIR ruling which the Court considered as a "general interpretative rule" issued in accordance with Section 4 of the Tax Code,[43] the Court has carved out exceptions in the application of the two-year and the "120+30" day periods. The Court synthesized these rules in *Visayas Geothermal Power Co., v. Commissioner of Internal Revenue*,[44] as follows:

> For clarity and guidance, the Court deems it proper to outline the rules laid down in *San Roque* with regard to claims for refund or tax credit of unutilized creditable input VAT. They are as follows:
>
> 1. When to file an administrative claim with the CIR:
>
> a. General rule — Section 112(A) and *Mirant*
>
> Within 2 years from the close of the taxable quarter when the sales were made.
>
> b. Exception — *Atlas*

---

[40] Applied Food Ingredients Co., Inc. v. Comm'r of Internal Revenue, G.R. No. 184266, 709 SCRA 164, 174, Nov. 11, 2013.

[41] [Hereinafter "*San Roque*"], G.R. No. 187485, 690 SCRA 336, Feb. 12, 2013.

[42] *See* Atlas Consol. Mining & Dev. Corp. v. Comm'r of Internal Revenue, G.R. No. 146221, 534 SCRA 51, Sept. 25, 2007; Comm'r of Internal Revenue v. Mirant Pagbilao Corp., G.R. No. 172129, 565 SCRA 154, Sept. 12, 2008; *and Aichi,* 632 SCRA 422.

[43] *See* BIR Rul. No. DA-489-03 (2003).

[44] G.R. No. 197525, 725 SCRA 130, June 4, 2014.

> Within 2 years from the date of payment of the output VAT, if the administrative claim was filed from June 8, 2007 (promulgation of *Atlas*) to September 12, 2008 (promulgation of *Mirant*).

2. When to file a judicial claim with the CTA:

   a. General rule — Section 112(D); not Section 229

      i. Within 30 days from the full or partial denial of the administrative claim by the CIR; or

      ii. Within 30 days from the expiration of the 120-day [now 90-day] period provided to the CIR to decide on the claim. This is mandatory and jurisdictional beginning January 1, 1998 (effectivity of 1997 NIRC).

   b. Exception — BIR Ruling No. DA-489-03

      > The judicial claim need not await the expiration of the 120-day period, if such was filed from December 10, 2003 (issuance of BIR Ruling No. DA-489-03) to October 6, 2010 (promulgation of *Aichi*).[45]

Another landmark decision rendered by the Supreme Court *en banc* is the case of *Pilipinas Total Gas, Inc. v. Commissioner of Internal Revenue*[46] where the Court clarified the issue of the reckoning point within which the "120+30" day period shall commence. Under Section 112(C) of the Tax Code, the 120-day (now 90-day) period within which the Commissioner shall decide on the refund claim commences from the submission of complete documents (now official receipts, invoices, and other supporting documents) in support of the application for refund. The Court ruled that it is the taxpayer who decides on the completeness of the documents supporting the refund claim, as he or she has the right and burden to forward such claim.[47] For refund claims filed before June 11, 2014, the taxpayer is entitled 30 days from the filing of the refund claim within which to submit the complete documents. But with the issuance of Revenue Memorandum Circular No. 54-2014 (carried over to the

[45] *Id.* at 149-150.
[46] G.R. No. 207112, 776 SCRA 395, Dec. 8, 2015.
[47] *Id.* at 417.

present under RMC No. 17-2018), all refund claims must be accompanied by complete supporting documents, as no other documents shall be submitted thereafter.[48]

II. INTEREST

A. Concept of Interest

Interest is based on the financial principle that the cost of money today would not be the same in the future because the peso now can be invested and earn positive returns—this is called the *time value of money*.[49] This concept of interest is what is called *monetary* interest, or the "compensation fixed by the parties for the use or forbearance of money."[50] The usual loan contract may have stipulations imposing this kind of interest,[51] which must be expressly stated in writing to be enforceable,[52] and must not be unconscionable.[53] On the other hand, interest may also be imposed by law or by the courts as penalty or indemnity for damages, which is called *compensatory* or *penalty* interest.[54] Even though not stipulated in writing, compensatory interest of 6% per annum may be imposed when the debtor incurs delay in the repayment of a sum of money,[55] or it may likewise be imposed on the monetary interest due from the time it is judicially demanded.[56]

For easy understanding on how interest is computed and applied, particularly with regard to interest in the concept of actual or compensatory damages, reference is made to the seminal cases of *Eastern Shipping Lines, Inc. v. Court of Appeals*,[57] *Nacar v. Gallery Frames*,[58] and the recent decision in *Lara's Gifts & Decors, Inc. v. Midtown Industrial Sales, Inc.*,[59] where the Court synthesized all statutory rules on the imposition of interest, as follows:

---

[48] *Id.* at 419.

[49] LAWRENCE J. GITMAN, PRINCIPLES OF MANAGERIAL FINANCE 162 (12th ed. 2009).

[50] Siga-an v. Villanueva [hereinafter "*Siga-an*"], G.R. No. 173227, 576 SCRA 696, 704, Jan. 20, 2009.

[51] CIVIL CODE, art. 1933.

[52] Art. 1956.

[53] *Abella*, 762 SCRA 221, 239. "The imposition of an unconscionable interest rate is void *ab initio* for being 'contrary to morals, and the law.'"

[54] *Siga-an*, 576 SCRA at 704.

[55] CIVIL CODE, art. 2209.

[56] Art. 2212.

[57] G.R. No. 97412, 234 SCRA 78, July 12, 1994.

[58] [Hereinafter "*Nacar*"], G.R. No. 189871, 703 SCRA 439, Aug. 13, 2013.

[59] G.R. No. 225433, Aug. 28, 2019.

With regard to an award of interest in the concept of actual and compensatory damages, the rate of interest, as well as the accrual thereof, is imposed, as follows:

1. When the obligation is breached, and it consists in the payment of a sum of money, *i.e.*, a loan or forbearance of money, goods, credits or judgments, the interest due shall be that which is stipulated by the parties in writing, provided it is not excessive and unconscionable, which, in the absence of a stipulated reckoning date, shall be computed from default, *i.e.*, from extrajudicial or judicial demand in accordance with Article 1169 of the Civil Code, UNTIL FULL PAYMENT, without compounding any interest unless compounded interest is expressly stipulated by the parties, by law or regulation. Interest due on the principal amount accruing as of judicial demand shall SEPARATELY earn legal interest at the prevailing rate prescribed by the [BSP], from the time of judicial demand UNTIL FULL PAYMENT.

2. In the absence of stipulated interest, in a loan or forbearance of money, goods, credits or judgments, the rate of interest on the principal amount shall be the prevailing legal interest prescribed by the [BSP], which shall be computed from default, *i.e.*, from extrajudicial or judicial demand in accordance with Article 1169 of the Civil Code, UNTIL FULL PAYMENT, without compounding any interest unless compounded interest is expressly stipulated by law or regulation. Interest due on the principal amount accruing as of judicial demand shall SEPARATELY earn legal interest at the prevailing rate prescribed by the [BSP], from the time of judicial demand UNTIL FULL PAYMENT.

3. When the obligation, not constituting a loan or forbearance of money, goods, credits or judgments, is breached, an interest on the amount of damages awarded may be imposed in the discretion of the court at the prevailing legal interest prescribed by the [BSP], pursuant to Articles 2210 and 2011 of the Civil Code. No interest, however, shall be adjudged on unliquidated claims or damages until the demand can be established with reasonable certainty. Accordingly, where the amount of the claim or damages is established with reasonable certainty, the prevailing legal interest shall begin to run from the time the claim is made extrajudicially or judicially (Art. 1169, Civil Code) UNTIL FULL PAYMENT, but when such certainty cannot be so reasonably established at the time the demand is made, the interest shall begin to run only from the date of the judgment of the trial court (at which time the quantification of damages may be deemed to have been reasonably ascertained) UNTIL FULL PAYMENT. The actual base for the computation of the interest shall, in any case, be on the principal

> amount finally adjudged, without compounding any interest unless compounded interest is expressly stipulated by law or regulation.[60]

Lara's Gifts provides for the current guidelines on the imposition of interest, especially with regard to interest in the concept of damages, by synthesizing the different provisions of the Civil Code and related jurisprudence on loans, forbearance of money, credits, and judgments. It is especially useful in the succeeding discussion on how interest is to be applied and computed for tax refunds.

B. Interest in Tax Refund Cases

In order to analyze whether interest may be imposed on tax refund cases, a discussion of the concept of *solutio indebiti* is indispensable. *Solutio indebiti* traces its roots to the ancient principle that no one shall enrich himself or herself unjustly at the expense of another.[61] Article 2154 of the Civil Code is the statutory basis for this quasi-contract, which provides that "if something is received when there is no right to demand it, and it was unduly delivered through mistake, the obligation to return it arises. In such a case, a creditor-debtor relationship is created under a quasi-contract whereby the payor becomes the creditor who then has the right to demand the return of payment made by mistake, and the person who has no right to receive such payment becomes obligated to return the same."[62] Jurisprudence has provided for two requisites needed to prove the existence of *solutio indebiti*, namely: (1) the absence of a right to collect the excess sums; and (2) that the payment was made by mistake.[63]

There are competing jurisprudence on whether the quasi-contract of *solutio indebiti* is applicable in tax refund cases. In *Commissioner of Internal Revenue v. Acesite (Philippines) Hotel Corporation*,[64] the Court ruled that tax refunds are based on *solutio indebiti*, *viz.*:

> Tax refunds are based on the principle of quasi-contract or *solutio indebiti* and the pertinent laws governing this principle are found in Arts. 2142 and 2154 of the Civil Code[.]

---

[60] *Id.* (Capitalization in the original.)

[61] Dom. Petroleum Retailer Corp. v. Manila Int'l Airport Auth., G.R. No. 210641, 898 SCRA 556, 569, Mar. 27, 2019, *citing* Power Comm'l and Industrial Corp. v. Ct. of Appeals, 340 Phil. 705, 718 (1997).

[62] *Siga-an*, 576 SCRA 696, 708.

[63] Titan-Ikeda Constr. & Dev. Corp. v. Primetown Prop. Group, Inc., G.R. No. 158768, 544 SCRA 466, 484, Feb. 12, 2008, *citing* Velez v. Balzarza, 73 Phil. 630, 632 (1942).

[64] G.R. No. 147295, 516 SCRA 93, Feb. 16, 2007.

* * *

> When money is paid to another under the influence of a mistake of fact, that is to say, on the mistaken supposition of the existence of a specific fact, where it would not have been known that the fact was otherwise, it may be recovered. The ground upon which the right of recovery rests is that money paid through misapprehension of facts belongs in equity and in good conscience to the person who paid it.
>
> The Government comes within the scope of *solutio indebiti* principle [...] where we held that: "Enshrined in the basic legal principles is the time-honored doctrine that no person shall unjustly enrich himself at the expense of another. It goes without saying that the Government is not exempted from the application of this doctrine."[65]

In the subsequent case of *State Land Investment Corp. v. Commissioner of Internal Revenue*,[66] and as similarly adopted in the recent case of *Philippine Airlines, Inc. v. Commissioner of Internal Revenue*,[67] the Court premised the applicability of *solutio indebiti* to tax refunds as a matter of substantial justice, to wit:

> Technicalities and legalisms, however exalted, should not be misused by the government to keep money not belonging to it, thereby enriching itself at the expense of its law-abiding citizens. Under the principle of *solutio indebiti* provided in Art. 2154, Civil Code, the BIR received something "when there [was] no right to demand it," and thus, it has the obligation to return it. Heavily militating against [the] Commissioner is the ancient principle that no one, not even the state, shall enrich oneself at the expense of another. Indeed, simple justice requires the speedy refund of the wrongly held taxes.[68]

However, in other cases, the Supreme Court foreclosed the applicability of *solutio indebiti* in tax refund cases. In the case of *Commissioner of Internal Revenue v. Manila Electric Company*,[69] the Court ruled that:

> [P]etitioner is misguided when it relied upon the six (6)-year prescriptive period for initiating an action on the ground of quasi

---

[65] *Id.* at 102-103.
[66] G.R. No. 171956, 542 SCRA 114, Jan. 18, 2008.
[67] G.R. No. 206079, 851 SCRA 518, Jan. 17, 2018.
[68] *Id.* at 567-68.
[69] *MERALCO*, 725 SCRA 384.

> contract or *solutio indebiti* under Article 1145 of the New Civil Code. There is *solutio indebiti* where: (1) payment is made when there exists no binding relation between the payor, who has no duty to pay, and the person who received the payment; and (2) the payment is made through mistake, and not through liberality or some other cause. Here, there is a binding relation between petitioner as the taxing authority in this jurisdiction and respondent MERALCO which is bound under the law to act as a withholding agent of NORD/LB Singapore Branch, the taxpayer. Hence, the first element of *solutio indebiti* is lacking. Moreover, such legal precept is inapplicable to the present case since the Tax Code, a special law, explicitly provides for a mandatory period for claiming a refund for taxes erroneously paid.[70]

This ruling was later adopted in *Metropolitan Bank & Trust Company v. Commissioner of Internal Revenue*[71] where the Court held the inapplicability of *solutio indebiti* with tax refund cases since the Tax Code is a special law. However, with the disquisitions in the aforementioned cases, jurisprudence on the matter can be harmonized.

First, there is a need to distinguish again the kind of refund the taxpayer is claiming. For recovery of erroneously or illegally collected tax, the taxpayer initially paid a tax which under the law he is not obligated to pay. When such payment is made, the government thus holds something to which it has no right. Admittedly, the principle of *solutio indebiti* fits perfectly into this category. This is confirmed in the case of *Commissioner of Internal Revenue v. Fortune Tobacco Corp.*,[72] where the Supreme Court held that:

> Under the Tax Code itself, apparently in recognition of the pervasive quasi-contract principle [of *solutio indebiti*], a claim for tax refund may be based on the following: (a) erroneously or illegally assessed or collected internal revenue taxes; (b) penalties imposed without authority; and (c) any sum alleged to have been excessive or in any manner wrongfully collected.[73]

As can be seen, the grounds for the application of *solutio indebiti* are the instances of erroneous or illegal collection of tax explicitly provided under Sections 204(C) and 229 of the Tax Code. Thus, *solutio indebiti* applies in cases of recovery of erroneously or illegally collected tax.

---

[70] *Id.* at 399.

[71] G.R. No. 182582, 822 SCRA 496, Apr. 17, 2017.

[72] G.R. No. 167274, 559 SCRA 160, July 21, 2008.

[73] *Id.* at 184.

Importantly, *solutio indebiti*, as a quasi-contract, is subject to interest, as provided for in the Civil Code. Article 2159 thereof provides that, "[w]hoever in bad faith accepts an undue payment, shall pay legal interest if a sum of money is involved[.]" Thus, bad faith is a requisite for the imposition of interest in cases of *solutio indebiti*. The opposite of bad faith, good faith, is a broad standard to begin with. It is undefined in Philippine statute books, but jurisprudence may be able to shed light on its parameters:

> Good faith is an intangible and abstract quality with no technical meaning or statutory definition, and it encompasses, among other things, an honest belief, the absence of malice and the absence of design to defraud or to seek an unconscionable advantage. It implies honesty of intention, and freedom from knowledge of circumstances which ought to put the holder upon inquiry. The essence of good faith lies in an honest belief in the validity of one's right, ignorance of a superior claim and absence of intention to overreach another.[74]

Bad faith "implies a conscious and intentional design to do a wrongful act for a dishonest purpose or moral obliquity."[75] Thus, when an act is arbitrary, or done on a whim or without legal justification, bad faith is exhibited. As will be discussed hereafter, when the collection of the tax is tainted with arbitrariness, interest is imposable.

In the case of *Siga-an v. Villanueva*, the Supreme Court ruled that since the obligation arose from *solutio indebiti*, which is neither a loan nor forbearance of money, then it shall accrue interest at the legal rate.[76] This was later amplified in the case of *Abella v. Abella*, where the Court held that obligations arising from a quasi-contract are not obligations constituting a loan or forbearance of money; thus, interest may be imposed at the discretion of the court at the rate of 6% *per annum*.[77] The law and jurisprudence hold that quasi-contracts, like *solutio indebiti*, are subject to interest as applied in the guidelines provided for in *Lara's Gifts*. Tax refunds for recovery of erroneously or illegally collected tax, being in the nature of *solutio indebiti*, should then be subject to interest.

Second, if the refund of erroneously or illegally collected tax is considered *solutio indebiti*, then how about refunds of excess and unutilized input VAT? To recall once more, excess input taxes are not erroneously or

---

[74] Ochoa v. Apeta, G.R. No. 146259, 533 SCRA 235, 240, Sept. 13, 2007.
[75] Montinola v. Phil. Airlines, G.R. No. 198656, 734 SCRA 439, 458, Sept. 8, 2014.
[76] *Siga-an,* 576 SCRA 696, 711.
[77] *Abella*, 762 SCRA 221, 248.

illegally collected taxes. Hence, the disquisitions in the seminal case of *San Roque* are enlightening, *viz.*:

> The input VAT is not "excessively" collected as understood under Section 229 because at the time the input VAT is collected the amount paid is correct and proper. The input VAT is a tax liability of, and legally paid by, a VAT-registered seller of goods, properties or services used as input by another VAT-registered person in the sale of his own goods, properties, or services. This tax liability is true even if the seller passes on the input VAT to the buyer as part of the purchase price. The second VAT-registered person, who is not legally liable for the input VAT, is the one who applies the input VAT as credit for his own output VAT. If the input VAT is in fact "excessively" collected as understood under Section 229, then it is the first VAT-registered person—the taxpayer who is legally liable and who is deemed to have legally paid for the input VAT—who can ask for a tax refund or credit under Section 229 as an ordinary refund or credit outside of the VAT System. In such event, the second VAT-registered taxpayer will have no input VAT to offset against his own output VAT.
>
> In a claim for refund or credit of "excess" input VAT under Section 110(B) and Section 112(A), the input VAT is not "excessively" collected as understood under Section 229. At the time of payment of the input VAT the amount paid is the correct and proper amount. Under the VAT System, there is no claim or issue that the input VAT is "excessively" collected, that is, that the input VAT paid is more than what is legally due. The person legally liable for the input VAT cannot claim that he overpaid the input VAT by the mere existence of an "excess" input VAT. The term "excess" input VAT simply means that the input VAT available as credit exceeds the output VAT, not that the input VAT is excessively collected because it is more than what is legally due. Thus, the taxpayer who legally paid the input VAT cannot claim for refund or credit of the input VAT as "excessively" collected under Section 229.[78]

Apparently, since the input tax is not one that is excessively collected under Section 229 of the Tax Code, the principle of *solutio indebiti* does not apply. The collection of excess input VAT does not partake of an erroneous or illegal collection of tax, precisely because there was no error on the part of the BIR in collecting it. It is only because of the circumstance that the taxpayer has incurred zero-rated sales that subjected its output VAT at 0%.

---

[78] *San Roque*, 690 SCRA 336, 392–94.

If refunds of excess and unutilized input tax are not considered as *solutio indebiti*, does that mean that such refunds would not be subjected to interest? In the subsequent discussion herein, refunds of excess and unutilized input tax may be subject to interest not based on the principle of *solutio indebiti*, but on the general concept of damages, applying the Arbitrariness Test.

Third, as already discussed, there are several cases which provide that *solutio indebiti* is not applicable for tax refunds. But it is important to analyze the situations surrounding them. For example, in the *MERALCO* case, the issue was whether the prescriptive period of six years grounded upon the cause of *solutio indebiti*[79] was applicable for recovery of tax erroneously or illegally collected. The Supreme Court ruled that the six-year prescriptive period for quasi-contracts is inapplicable because the Tax Code, a special law, specifically provides for a mandatory period for claiming tax refunds.

Likewise, the disquisitions of the Court in *MERALCO* in saying that *solutio indebiti* does not apply to tax refunds, because there is a binding relation between the taxpayer and the taxing authority, does not take into consideration the specific instances that create such relation. Even though tax is in its nature ubiquitous,[80] it is not always the case that a person is subject to tax. The tax should depend on the transaction at hand. For if the transaction does not call for the payment of tax, then there is no legal relationship between the person and the taxing authority, simply because there is no obligation to pay the tax. For example, when a taxpayer pays a tax for which it is exempt under the law, there is no relation established between the taxpayer and the BIR because the law does not create one. This is precisely the case when it comes to the recovery of tax erroneously or illegally collected. There is no legal authority that justifies the collection or provides that the collection was made in excess of what the law prescribes, thus rendering the statement in *MERALCO* quite specious. Moreover, in the recent case of *San Miguel*, the Court acknowledged that tax refunds are indeed grounded on the principle of *solutio indebiti*, but when it comes to the prescriptive period that should be followed, it is the Tax Code which controls as the special law, and the Tax Code prevails over the general law, which is the Civil Code.[81] Thus, jurisprudence may be harmonized by concluding that the principle of *solutio*

---

[79] CIVIL CODE, art. 1145.

[80] Madsen Pirie, *Death and Taxes*, ADAM SMITH INSTITUTE WEBSITE, *available at* https://www.adamsmith.org/blog/death-and-taxes (last accessed Oct. 4, 2020). "Benjamin Franklin wrote in a letter [...] a phrase that has reverberated ever since: [...] [B]ut in this world nothing can be said to be certain, except death and taxes."

[81] This is the principle of *generalia specialibus non derogant* in statutory construction. *See, e.g.*, Phil. Nat'l Oil Co. v. Ct. of Appeals, G.R. No. 109976, 457 SCRA 32, 80, Apr. 26, 2005.

indebiti applies to the recovery of tax erroneously or illegally collected, but the applicable prescriptive period is that found in the Tax Code, not the Civil Code.

III. PRESENT RULE ON INTEREST IN TAX REFUNDS

So, what keeps the courts from imposing the concomitant interest in tax refund cases? An examination of the statutory and legal bases is in order.

A. Statutory Basis

Currently, there is no provision in the Tax Code which explicitly provides for the imposition of interest in tax refunds. The interest imposed in the Tax Code is that of *deficiency* and *delinquency* interest imposed on tax assessments.[82] The rate of deficiency and delinquency interest is currently pegged at double the legal rate for loans or forbearance of money, or 12%.[83] Before the enactment of TRAIN, deficiency and delinquency interest were at 20%, and they could be imposed simultaneously. Under TRAIN, unpaid tax assessments are imposed the lesser rate of 12%, and there is a proviso which prohibits their simultaneous imposition.[84] But more importantly, there is a lack of any provision on the imposition of interest in tax refunds. Since there is no mention in the Tax Code of interest on tax refunds, there is also no express or implied prohibition for its imposition. It is a basic rule of statutory interpretation that "what is not expressly or impliedly prohibited by law may be done, except when the act is contrary to morals, customs, and public order."[85] It would be far-fetched to presume that the imposition of interest, which is usual especially for loan contracts and which the Civil Code expressly governs, could be considered as contrary to morals, customs, or public order. In some decided cases of the Supreme Court, it was ruled that it is the unconscionable *rate* of interest that is against morals, customs, or public order, and not the mere fact of its *imposition*.[86]

---

[82] TAX CODE, § 249.

[83] Revenue Reg. No. 21–2018 (2018), § 2.

[84] TAX CODE, § 249(A).

[85] Manila Elec. Co. v. Public Service Comm'n, 60 Phil. 658, 661 (1934).

[86] *See, e.g.*, De la Paz v. L & J Dev. Co., G.R. No. 183360, 734 SCRA 364, 376–77, Sept. 8, 2014. "Time and again, it has been ruled in a plethora of cases that stipulated interest rates of 3% per month and higher, are excessive, iniquitous, unconscionable and exorbitant. Such stipulations are void for being contrary to morals, if not against the law."

B. Jurisprudential Basis

If the current Tax Code does not mention interest on tax refunds in any of its provisions, does that preclude its imposition? Apparently, there is jurisprudential basis for the imposition of interest. In the resolution of the case in *Carcar Electric & Ice Plant Co., Inc. v. Collector of Internal Revenue*,[87] the Supreme Court ruled that interest is imposable on tax refunds. Quoted hereunder is the discussion of the Supreme Court on the matter, thus:

> Turning now to the question of the Collector's liability for interest on taxes improperly collected: Under the Internal Revenue Act of 1914, the Collector of Internal Revenue was held liable for such interests (Hongkong Shanghai Bank vs. Rafferty, 39 Phil. 153; Heacock Co. vs. Collector of Customs, 37 Phil. 970; Vda. e Hijos de P. Roxas vs. Rafferty, 37 Phil. 957, and authorities cited therein) in the absence of any exempting provision in the law, and on the strength of American authorities to the effect that the State's exemption from paying interest on its obligations was never applied to subordinate governmental agencies. In Heacock Co. vs. Collector of Customs, supra, p. 980–981, this Court said:
>
> > "While the sovereign State, in the absence of statute or contract, is not liable to pay interest, it has been held, however, that governmental agencies, whether individuals or boards, which have been given the power to sue and to defend suits may be compelled to pay interest upon their indebtedness even though the Government itself ultimately pays the indebtedness. Tax collectors are almost universally given the power to defend suits against them for illegal collection of taxes. It is usually provided that the person taxed may protest and appeal to the courts to have the question of the legality of the assessment determined. It is usually provided that when the courts determine that assessment was illegal, the Government itself will refund the money, relieving the collector of personal liability. (See Section 989, Revised Statutes of the United States.)
>
> In the case of Erskine vs. Van Arsdale (15 Wall. [U.S.], 68–75), the Supreme Court of the United States held that—
>
> > 'Taxes illegally assessed and paid may always be recovered back, if the collector understands from the payer that the taxes are regarded as illegal and that suit will be instituted to compel the refunding of them. * * * Where an illegal tax has been collected, the citizen who has paid it, and has been obliged to bring suit against the collector, is, we think, entitled to interest in the event of recovery, from the time of the illegal exaction."

---

[87] [Hereinafter "*Carcar*"], 100 Phil. 50 (1956).

> (See also Schell vs. Crockren, 107 U.S., 625; National Home vs. Parrish, 229 U.S., 196; White vs. Arthur, 10 Fed. Rep. 80; McClain vs. Pennsylvania Company, 108 Federal Republic 618.)

In the case of National Rome vs. Parrish (229 U.S., 496), the Supreme Court, discussing the question before us, said:

> 'It is quite true that the United States cannot be subjected to the treasury. (Erskine vs. Van Arsdale, 15 Wall., [U.S.], 68–75; to pay it or a statute permitting its recovery. (U.S. Ex rel. Angarica vs. Bayard, 127 U.S., 251; U.S. vs. State of North Carolina, 136 U.S., 211.) But this exemption has never as yet been applied to subordinate governmental agencies. On the contrary, in suits against collectors to recover moneys illegally exacted as taxes and paid under protest, the settled rule is that interest is recoverable without any statute to that effect, and this although the judgment is not to be paid by the collector, but directly from the treasury. (Erskine vs. Van Arsdale, 15 Wall. [U.S.], 68–75; Redfield vs. Bartels, 139 U.S. 694)'"

Subsequently, section 1579 of the Administrative Code of 1917 (Act 2711) expressly authorized suits against the Collector of Internal Revenue "for the recovery without interest of the sum alleged to have been illegally collected," and thereafter, no judgments for interest were rendered against the Collector. But in 1939, the National Internal Revenue Code came into effect and its section 306 authorized recovery of taxes erroneously or illegally collected, but omitting the expression "without interest" employed in section 1579 of the 1917 Administrative Code that it superseded. Considering the repeated holdings of this Court that in the absence of words of exemption the Collector was liable for interest on taxes improperly collected, the legislature's failure to reenact the words "without interest" of the Administrative Code of 1917 imparted a desire to return to the rule in force before 1917 and under the Internal Revenue Act of 1914. This view is supported by sec. 310 of the National Internal Revenue Code, as follows:

> "SEC. 310. Satisfaction of judgment recovered against treasurer or other officer.—When an action is brought against any revenue officer to recover damages by reason of any act done in the performance of official duty, and the Collector of Internal Revenue is notified of such action in time to make defense against the same, through the Solicitor-General, any judgment, damages, or costs recovered in such action shall be satisfied by the Collector of Internal Revenue upon approval of the Department Head, or if the same be paid by the person sued, shall be repaid or reimbursed to him."

> As observed by this Court in Heacock Co. vs. Collector of Customs, 37 Phil. 970, 982, the damages for wrongful exaction of money is precisely interest at the legal rate:
>
> > "Section 144 of the Internal Revenue Act of 1914 authorizes the Collector of Internal Revenue, in cases like the present, to pay out of public funds in his hands 'any judgment, damages, or costs' recovered in an action brought against 'any revenue officer' by reason of any act done in the performance of official duties. The "damages" for the wrongful exaction or withholding of money is the payment of interest at the legal rate. (Article 1108, Civil Code.)"
>
> We conclude that under the present Internal Revenue Code the Collector of Internal Revenue may be made to answer for interest at the legal rate on taxes improperly collected. Such liability serves as additional safeguard in favor of the taxpayer against arbitrariness in the exaction or collection of taxes and imposts.[88]

The quoted segment in *Carvar* shall be dissected to fully analyze the jurisprudential mooring it brings. *Carvar* consistently references the case of *H.E. Heacock Co. v. Insular Collector of Customs*,[89] which laid down the rule that "[t]he exemption of the sovereign state does not apply in actions against collectors to recover moneys illegally exacted as taxes and paid under protest. The settled rule is that interest is recoverable without any statute to that effect, and this although the judgment is not to be paid by the collector but directly from the treasury."[90] *Heacock* was decided under the aegis of the Tariff Act of 1909 passed by the US Congress. Nevertheless, the Supreme Court laid down the principle that in the absence of a statute to pay interest, the government is not liable to pay such, except for tax illegally exacted from taxpayers. Borrowing from US jurisprudence, the Court laid down the rule that the payment of interest is allowed in tax refunds.[91]

---

[88] *Id.* at 57–60.

[89] 37 Phil. 970 (1918).

[90] *Id.* at 981.

[91] Philippine tax laws originated from US tax laws. The origin of the country's current Tax Code started with the Internal Revenue Law of 1904, *see* Act No. 1189 (1904), which was patterned after the tax laws of the United States. The Internal Revenue Law of 1904 would subsequently undergo further changes, and it was until the enactment of the National Internal Revenue Code of 1939, Comm. Act No. 466 (1939), that the first codification of the country's tax laws began. The 1939 Tax Code would be overhauled in 1977, *see* Pres. Dec. No. 1158 (1977), and then in 1997, the basis of the current Tax Code. *See* Comm'r of Internal Revenue v. Ct. of Appeals, G.R. No. 108576, 301 SCRA 152, 173, Jan. 20, 1999. "Having been derived from a foreign law, resort to the jurisprudence of its origin may shed light."

But *Carcar* did not rely on US jurisprudence alone. It likewise traced the history of the applicable laws. *Carcar* noted that under the old Administrative Code of 1917,[92] tax refund suits may be lodged against the Collector of Internal Revenue (predecessor of the Commissioner) for the recovery of the tax "without interest." However, Section 310 of the 1939 Tax Code removed the phrase "without interest." The Court interpreted this omission as the legislature's intent to do away with the rule under the old Administrative Code that interest cannot be claimed in tax refund cases. Significantly, Section 227 of the current Tax Code, which is based on Section 310 of the 1939 Tax Code, also does not contain the provision "without interest." It is a rule in statutory construction that an amendment by the deletion of words or phrases indicates an intention to change the statutory meaning.[93] With the deletion of the phrase "without interest" in the 1939 Tax Code, an amendment carried over into the present Tax Code, the authors of the law deemed it best to continue the interpretation that interest may be claimed in tax refunds.

Carcar likewise held that interest is a form of "damages" paid for the wrongful exaction or withholding of money by the BIR. Section 227 of the present Tax Code likewise provides for this, the only difference being that there is now a proscription that no "damages" shall be paid if the taxpayer acted negligently or in bad faith, or with willful oppression.

However, subsequent to *Carcar*, the Court in *Collector of Internal Revenue v. St. Paul's Hospital of Iloilo*[94] succinctly said that, "[i]n the absence of a statutory provision clearly or expressly directing or authorizing such payment, and none has been cited, the National government cannot be required to pay interests."[95] Without expounding on this new principle, and without expressly overturning the doctrine laid down in *Carcar*, the Court simply opined that a statutory provision is needed to impose interest on tax refunds. Thus, the Court laid down a principle in conflict with precedent, but did not abandon or reverse the latter.

Thereafter, in the cases of *Collector of Internal Revenue v. Sweeney*,[96] *Commissioner of Customs v. Borres*,[97] and *Collector of Internal Revenue v. Fisher*,[98] the

---

[92] Act No. 2711 (1917).

[93] Obiasca v. Basallote, G.R. No. 176707, 613 SCRA 110, 129, Feb. 17, 2010, *citing* Laguna Metts Co. v. Caalam, G.R. No. 185220, 594 SCRA 139, 145, July 27, 2009.

[94] [Hereinafter "*St. Paul's Hospital*"], 105 Phil. 1319 (1959).

[95] *Id.* at 1320.

[96] 106 Phil. 59 (1959).

[97] 106 Phil. 625 (1959).

[98] 110 Phil. 686 (1961).

Court echoed its pronouncement in *St. Paul's Hospital* that there is no statutory instruction authorizing the payment of interest in tax refunds, without any mention of the holding in *Carcar*.

Then, in *Collector of Internal Revenue v. Prieto*,[99] the Court had the opportunity to harmonize the conflicting rulings in *Carcar* and *St. Paul's Hospital*, *viz.*:

> Our decision in the Carcar case, however, must be understood as holding the Collector of Internal Revenue liable for interest on taxes improperly collected only if the collection was attended with "arbitrariness". The facts involved in the case relied upon by petitioner—the St. Paul's Hospital of Iloilo case—do not seem to justify the conclusion that arbitrariness attended or characterized the collection of the taxes in question therein. [. . .]
>
> * * *
>
> The question of whether or not the sale of drugs and medicines made at the pharmacy department of the St. Paul's Hospital of Iloilo were taxable was, in our opinion, a fairly debatable issue. The Collector, therefore, cannot be said to have acted arbitrarily in assessing the corresponding tax on the hospital. This being the case, we see no real conflict between our decision in the Carcar case, on the one hand, and the one rendered in the St. Paul's Hospital of Iloilo case.
>
> The question we now have to decide is whether the first or the second ruling is the one applicable to the present case. Upon consideration of the facts appearing of record we believe that it is the first. The Collector of Internal Revenue had no reason to insist in collecting the inheritance tax from respondents on the basis of the value of the properties allotted to each of them, in accordance with the project of partition submitted to and approved by the court without deducting therefrom the cash payments which, in accordance with their agreement with their coheirs, they had to pay to the latter for the purpose of making the share of each heir equal in value to that of the others—as ordained in the will of the deceased Doña Teresa Tuason y de la Paz, and as agreed among the heirs. What each of the respondents really received as his share in the estate of said deceased was the value of the properties allotted to each of them minus the cash payments each had to make in order to equalize their respective share with that of the other heirs. The collection of the inheritance taxes herein involved being clearly

---

[99] [Hereinafter "*Prieto*"], G.R. No. 11976, 3 SCRA 101, Sept. 26, 1961.

> unjustified, we are constrained, as already stated above, to hold the ruling in the Carcar case applicable to the present.[100]

Though the Court did not squarely say that the ruling in *St. Paul's Hospital* had been abandoned, the Court categorically stated that interest may be imposed, albeit on the condition that there is "arbitrariness." This may have been sourced from the last statement in *Carcar* that the imposition of interest "serves as additional safeguard in favor of the taxpayer against arbitrariness in the exaction or collection of taxes and imposts."[101] The case of *Prieto* thus modified the rules in *Carcar*—that interest may be imposed in tax refunds—and in *St. Paul's Hospital*—that there is no legal basis in imposing interest—by definitively ruling that interest is imposable only when the collection of tax is tainted with arbitrariness.

However, succeeding decisions of the Court continued to invoke *Carcar*, *St. Paul's Hospital*, and *Prieto* in a manner that was confusing. Citing all these cases at once problematic since it presents a contradictory picture of the basis on which interest may be imposed in tax refund cases. If the Court cites *St. Paul's Hospital*, it avers that interest is not imposable because there is no statutory authority for it. But if it invokes *Carcar* and *Prieto*, then what is the authority that allows the imposition of interest, even when there is arbitrariness on the part of the BIR? That is why, as will be discussed hereafter, the Supreme Court is invited to reexamine its ruling in *St. Paul's Hospital.*

An example of the contradiction created by invoking competing jurisprudence is the case of *Collector of Internal Revenue v. Binalbagan Estate, Inc.*,[102] where the Court held that:

> On several occasions, we ruled that in the absence of a statutory provision clearly directing or authorizing the payment of interest on the amount to be refunded to the taxpayer, the National Government cannot be required to pay interest. Later, however, we held that where the collection of the tax sought to be refunded was attended with arbitrariness, the Commissioner of Internal Revenue is liable to pay interest. In the case at bar, collection of the deficiency income tax was not arbitrary.[103]

The Court in the above case applied the arbitrariness standard as enunciated in *Prieto* in determining whether the Commissioner was liable to

---

[100] *Id.* at 102–104.
[101] *Carcar*, 100 Phil. 50, at 60.
[102] G.R. No. 12752, 13 SCRA 1, Jan. 30, 1965.
[103] *Id.* at 10.

pay interest. However, it continued to invoke the ruling laid down in *St. Paul's Hospital.* Thus, there is a dilemma if the collection of tax is tainted with arbitrariness, what is its statutory basis if the Court continues to rule that there is no statutory provision directing the payment of interest? It should only be one or the other—either there is no statutory authority for the imposition of interest, or there is statutory authority for its imposition, albeit only if there is arbitrariness.

The Supreme Court continued this pattern in subsequent cases. In *Atlas Fertilizer Corporation v. Commissioner of Internal Revenue*,[104] the Court ruled that:

> But the more important consideration is the well settled rule that in the absence of a statutory provision clearly or expressly directing or authorizing payment of interest on the amount to be refunded to taxpayer, the Government cannot be required to pay interest. Likewise, it is the rule that interest may be awarded only when the collection of tax sought to be refunded was attended with arbitrariness. Such circumstance is not present in the case at bar as the payment of compensating taxes in question was made freely and voluntarily and conformably with the partial exemption granted by Republic Act No. 901.[105]

Then in *Philex Mining Corporation v. Commissioner of Internal Revenue*,[106] and later in *Banco de Oro v. Republic*,[107] the Court held that "the rule is that no interest on refund of tax can be awarded unless authorized by law or the collection of the tax was attended by arbitrariness."[108] Thus, the standing rule is that of a contradictory nature—interest may not be imposed because there is no statute that authorizes it, but it may be imposed when there is arbitrariness even in the absence of such statute.

IV. REEXAMINATION OF THE RULE

As stated, there are two rules being followed: (1) no interest is imposable because there is no law that provides for it ("No Statutory Authority Test"); and (2) interest may be imposed if there is arbitrariness ("Arbitrariness Test"). As will be discussed hereafter, it is this Note's purpose

---

[104] G.R. No. 26686, 100 SCRA 556, Oct. 30, 1980.
[105] *Id.* at 568–69.
[106] [Hereinafter "*Philex*"], G.R. No. 120324, 306 SCRA 126, Apr. 21, 1999.
[107] [Hereinafter "*Banco de Oro*"], G.R. No. 198756, 800 SCRA 392, Aug. 16, 2016.
[108] *Id.* at 464.

to examine the rules on the imposition of interest in tax refunds, and to propose workable guidelines that may be used by the courts. It is advocated that the Supreme Court, sitting *en banc*,[109] reexamine said rules.

A. No Statutory Authority Test

St. Paul's Hospital laid down the rule that since there is no statutory provision in the Tax Code that allows for the imposition of interest in tax refunds, then the courts are constrained not to impose interest. An examination of the current Tax Code renders the premise true—yes, there is no provision that authorizes the imposition of interest, but it is also true that there is no provision that prohibits its imposition.

It is an established principle of statutory construction that laws must be harmonized to give effect to all of them. Courts are "enjoin[ed] [to] endeavor [...] to harmonize the provisions of a law or two laws so that each shall be effective."[110] Thus, it is not only through the examination of the Tax Code that harmonization can be achieved, but likewise through the analysis and interpretation of other statutory provisions on the imposition of interest, most of which are found in the Civil Code. While the Tax Code is a special law and the Civil Code is a general law, harmonization entails looking into the latter and not being limited to the former. If the special law is silent, the general law should prevail since the special law provides no exception to the general rule.[111] As the Court held in *Vinzons-Chato v. Fortune Tobacco Corporation*[112]:

> A general law and a special law on the same subject are statutes in *pari materia* and should, accordingly, be read together and harmonized, if possible, with a view to giving effect to both. The rule is that where there are two acts, one of which is special and particular and the other general which, if standing alone, would include the same matter and thus conflict with the special act, the special law must prevail since it evinces the legislative intent more clearly than that of a general statute and must not be taken as intended to affect the more particular and specific provisions of the earlier act, unless it is absolutely necessary so to construe it in order to give its words any meaning at all.[113]

---

[109] CONST., art. VIII, § 4(3). "[N]o doctrine or principle of law laid down by the court in a decision rendered *en banc* or in division may be modified or reversed except by the court sitting *en banc*."

[110] Valera v. Tuason, Jr., 80 Phil. 823, 827 (1948).

[111] Lichauco & Co., Inc. v. Apostol, 44 Phil. 138, 147 (1922).

[112] G.R. No. 141309, 525 SCRA 11, June 19, 2007.

[113] *Id.* at 20-21.

Again, the Tax Code is silent on the imposition of interest on tax refunds. Neither does the Tax Code expressly allow nor expressly prohibit it. Thus, to harmonize the laws, reference to the provisions of the Civil Code is proper.

From the foregoing discussion, recovery of erroneously or illegally collected tax is a form of *solutio indebiti* from which the government is not exempted. Thus, applying the rules on the imposition of interest enunciated in *Lara's Gifts*, for tax refunds covering the recovery of tax erroneously or illegally collected, which are neither loans nor forbearance of money, interest on the amount awarded may be imposed at the *discretion* of the court at the prevailing legal interest rate prescribed by the BSP, which is currently pegged at 6%.[114] Notably, the imposition of interest for this kind of tax refund is left to the sound discretion of the court, meaning that interest is not automatically imposed. Sound discretion does not mean that the judge has free rein to impose interest in a whimsical manner, but only when the ends of justice and fairness are met—*discenere per legem quid sit justum*.[115] Since the statutory provisions of the Civil Code on interest are applicable to the quasi-contract of *solutio indebiti* and the recovery of erroneously or illegally collected tax is a form of *solutio indebiti*, then, logically, the No Statutory Authority Test is lacking in justification.

B. Arbitrariness Test

If the Supreme Court ultimately abandons the No Statutory Authority Test, what remains is the Arbitrariness Test. The latter is the more appropriate standard that courts can use in exercising their sound judicial discretion on whether to impose interest.

1. Concept of Arbitrariness

According to Timothy Endicott, arbitrariness is "lack of reason," such that "[w]henever a government agency does anything wrong, it goes against reason."[116] This is a very general definition of arbitrariness that, if applied, would not provide for the exercise of sound discretion of the courts; as it entails that as long as the BIR was wrong in not granting the refund claim of the taxpayer, interest would be imposed. Thus, defining what arbitrariness

---

[114] BSP–MB Res. No. 796 (2013).

[115] Richard B. Spindle, *Judicial Discretion in Common Law Courts*, 4 WASH. & LEE. L. REV. 143, 144 (1947).

[116] Timothy Endicott, *Arbitrariness*, 27 CAN. J. L. & JURIS. 49, 49 (2014).

is, or what constitutes an arbitrary act, is important in providing workable guidelines for the imposition of interest.

Arbitrariness, in its plain meaning, pertains to "the quality of being based on chance rather than being planned or based on reason" or "the unfair and unlimited use of personal power."[117] In the case of *Philex*, arbitrariness was defined as something that "presupposes inexcusable or obstinate disregard of legal provisions."[118] The Court then defined arbitrariness in the negative: "[a]n action is not arbitrary when exercised honestly and upon due consideration where there is room for two opinions, however much it may be believed that an erroneous conclusion was reached."[119] Thus, the arbitrariness that the courts are mandated to examine is that which may taint the action of the Commissioner in collecting the tax and denying the claim for refund. It is the action or inaction of the Commissioner which is the subject of arbitrariness.

In the US, there exists a form of judicial review called the "arbitrary and capricious" standard used by the federal courts in reviewing the rulemaking and adjudicatory decisions of administrative agencies. It is based on the provisions of the Administrative Procedure Act (APA)[120] and best explained in the case of *Motor Vehicle Manufacturers Association of the United States, Inc. v. State Farm Mutual Automobile Insurance Co.*,[121] where the US Supreme Court held:

> The scope of review under the "arbitrary and capricious" standard is narrow, and a court is not to substitute its judgment for that of the agency. Nevertheless, the agency must examine the relevant data and articulate a satisfactory explanation for its action, including a "rational connection between the facts found and the choice made." [...] In reviewing that explanation, we must "consider whether the decision was based on a consideration of the relevant factors and whether there has been a clear error of judgment." [...] Normally, an agency rule would be arbitrary and capricious if the agency has relied on factors which Congress has not intended it to consider, entirely failed to consider an important aspect of the problem, offered an explanation for its decision that runs counter to the evidence before the agency, or is so implausible that it could

---

[117] *Arbitrariness*, CAMBRIDGE DICTIONARY, *available at* https://dictionary.cambridge.org/us/dictionary/english/arbitrariness (last accessed Sept. 24, 2020).

[118] *Philex*, 306 SCRA 126, at 134.

[119] *Id.*

[120] 60 Stat. 237 (1946).

[121] 463 U.S. 29 (1983).

> not be ascribed to a difference in view or the product of agency expertise.[122]

Although the "arbitrary and capricious" standard has not found total application to actions of the US Internal Revenue Service (IRS), the counterpart agency of the BIR, there have been legal commentators who have advocated for the use of the standard and the concomitant provisions of the APA to the agency actions of the IRS.[123] Some have also opined that the recent decisions of the federal Supreme and lower courts have made administrative law provisions, such as the APA, applicable to tax.[124] The US Court of Appeals for the District of Columbia Circuit has likewise ruled that "[t]he IRS is not special in this regard; no exception exists shielding it, unlike the rest of the Federal Government, from suit under the APA."[125] Thus, similar to the US, where the Philippines' tax laws originated, the general principles of administrative law may be made to apply to the functions of revenue agencies, notwithstanding provisions in the tax law that are specifically applicable.

Nevertheless, the elements that underlie "arbitrary and capricious" review continue to have equivalence with how acts of administrative agencies in the Philippines are to be measured. To emphasize, one of the primary considerations in "arbitrary and capricious" review, which is similar in this jurisdiction, is the function of the court to examine whether there is satisfactory explanation for the agency action, or simply that the action should have been based on the facts and the law and that the agency must sufficiently provide factual and legal bases for its decision, as supported by substantial evidence.[126]

Relative thereto, the Philippine Supreme Court has long articulated the elements of procedural due process in administrative proceedings, as enshrined in the landmark case of *Ang Tibay v. Court of Industrial Relations*,[127] to wit:

> There are cardinal primary rights which must be respected even in proceedings of this character:

---

[122] *Id.* at 43.

[123] Rimma Tsvasman, *No More Excuses: A Case for the IRS' Full Compliance with the Administrative Procedure Act*, 76 BROOK. L. REV. 837 (2011).

[124] Steve R. Johnson, *Reasoned Explanation and IRS Adjudication*, 63 DUKE L.J. 1771, 1773 (2014).

[125] Cohen v. United States, 650 F.3d 717, 723 (D.C. Cir. 2011).

[126] *See* Solid Homes, Inc. v. Laserna, G.R. No. 166051, 550 SCRA 613, 627, Apr. 8, 2008.

[127] 69 Phil. 635 (1940).

(1) The first of these rights is the right to a hearing, which includes the right of the party interested or affected to present his own case and submit evidence in support thereof. [. . .]

(2) Not only must the party be given an opportunity to present his case and to adduce evidence tending to establish the rights which he asserts but the tribunal must consider the evidence presented. [. . .]

(3) "While the duty to deliberate does not impose the obligation to decide right, it does imply a necessity which cannot be disregarded, namely, that of having something to support its decision. A decision with absolutely nothing to support it is a nullity, a place when directly attached." [. . .]

(4) Not only must there be some evidence to support a finding or conclusion [. . .] but the evidence must be "substantial." [. . .] "Substantial evidence is more than a mere scintilla. It means such relevant evidence as a reasonable mind might accept as adequate to support a conclusion."

(5) The decision must be rendered on the evidence presented at the hearing, or at least contained in the record and disclosed to the parties affected. [. . .] Only by confining the administrative tribunal to the evidence disclosed to the parties, can the latter be protected in their right to know and meet the case against them. It should not, however, detract from their duty actively to see that the law is enforced, and for that purpose, to use the authorized legal methods of securing evidence and informing itself of facts material and relevant to the controversy.

(6) The [administrative agency] or any of its [officers], therefore, must act on its or his own independent consideration of the law and facts of the controversy, and not simply accept the views of a subordinate in arriving at a decision. [. . .]

(7) The [administrative agency] should, in all controversial questions, render its decision in such a manner that the parties to the proceeding can know the various issues involved, and the reasons for the decisions rendered. The performance of this duty is inseparable from the authority conferred upon it.[128]

---

[128] *Id.* at 642–44.

In addition, the Administrative Code of 1987 provides for the rules administrative agencies are required to follow in exercising both their rule-making and adjudicatory functions, as the case may be. Notably, the foremost elements with respect to the adjudication function, all of which are statutory enshrinements of the principles laid down in *Ang Tibay*, are the "notice and hearing" requirement,[129] the observance of the substantive evidence standard,[130] and that decisions of administrative agencies should clearly state the facts and law on which they are based.[131]

The action of the Commissioner in deciding a claim for refund partakes of a quasi-judicial nature.[132] The exercise of quasi-judicial functions "applies to the action, discretion, etc. of public administrative officers or bodies, who are required to investigate facts, or ascertain the existence of facts, hold hearings, and draw conclusions from them, as a basis for their official action and to exercise discretion of a judicial nature."[133] In deciding on a tax refund claim, the Commissioner, or his or her duly authorized representative, investigates the facts by examining the evidence presented by the taxpayer and thereafter resolves whether such taxpayer is entitled to the refund being sought. As an administrative agency exercising adjudicatory powers, the BIR is not exempt from complying with the requisites of administrative due process enunciated in *Ang Tibay* and the applicable provisions of the Administrative Code on the matter. Thus, for example, when a taxpayer files a refund claim for recovery of erroneously or illegally collected tax and the Commissioner renders a decision within the applicable period denying the claim, but without any reference as to why the claim was denied, either in fact or in law, or both, then such decision violates the cardinal rules of administrative due process. Such decision is therefore a product of an arbitrary act on the part of the Commissioner for which interest is imposable.

As discussed, tax refunds in the form of recovery of erroneously or illegally collected tax are a form of *solutio indebiti* for which interest is imposable after applying the Arbitrariness Test. The other form of tax refund under the Tax Code, which is refund of excess and unutilized input tax, though not a

---

[129] Exec. Order No. 292 (1987), bk. VII, chap. 3, § 11.

[130] § 12(1).

[131] § 14.

[132] Comm'r of Internal Revenue v. Ct. of Tax Appeals, G.R. No. 207843, July 15, 2015. "Section 4 of the NIRC confers upon the CIR [...] the power to decide tax cases in the exercise of her quasi-judicial function."

[133] Monetary Board v. Phil. Veterans Bank, G.R. No. 189571, 746 SCRA 508, 518, Jan. 21, 2015, *citing* United Coconut Planters Bank v. E. Ganzon, Inc., G.R. No. 168859, 591 SCRA 321, 338, June 30, 2009.

form of *solutio indebiti*, may nevertheless be subject to interest applying the Arbitrariness Test.

In *Carcar*, the Supreme Court ruled that interest is a form of "damages" that may be awarded by the court to the taxpayer for which the revenue agency is liable under Section 144 of the Internal Revenue Act of 1914, and now under Section 227 of the current Tax Code. Interest is imposed in the concept of actual or compensatory damages, or "those awarded in order to compensate a party for an injury or loss he [or she] suffered. They arise out of a sense of natural justice, aimed at repairing the wrong done."[134] This means that interest is the damages awarded to the taxpayer for the government's unlawful withholding of money that is legally due the former. As held by the Court in *Nacar*, "[w]hen an obligation, regardless of its source, *i.e.*, law, contracts, quasi-contracts, delicts or quasi-delicts is breached, the contravenor can be held liable for damages."[135] Interest on tax refunds, whether for recovery of erroneously or illegally collected tax or for refund of excess and unutilized input tax, is imposed under the concept of compensatory damages governed by Articles 2209 and 2212 of the Civil Code.[136] Thus, the Court's guidelines enunciated in *Lara's Gifts* apply to the imposition of interest on tax refunds.

Specifically for the refund of excess and unutilized input tax, there is now a proviso in Section 112(C) of the Tax Code that mandates the Commissioner, in case there is a denial of the refund claim, to state in writing the factual and legal bases for such denial. This is in line with the administrative due process requirements in *Ang Tibay* and the instruction in Section 14, Chapter 3, Book VII of the Administrative Code, both of which provide that the decision of administrative agencies in the exercise of their quasi-judicial and adjudicatory functions should state therein the facts and the law on which it is based.

Section 112(C) of the Tax Code provides for a 90-day period for the Commissioner to act on the refund claim. If after the lapse of the period the Commissioner fails to act, the taxpayer may file the judicial claim before the CTA within 30 days from the lapse of the 90-day period. These periods are mandatory and jurisdictional on the part of the taxpayer,[137] and failure to

---

[134] Estrada v. Phil. Rabbit Lines, Inc., G.R. No. 203902, 831 SCRA 349, 374, July 19, 2017.

[135] *Nacar*, 703 SCRA 439, at 457.

[136] Sun Life of Canada (Phils.), Inc. v. Tan Kit, G.R. No. 183272, 738 SCRA 371, 381, Oct. 15, 2014.

[137] Hedcor, Inc. v. Comm'r of Internal Revenue, G.R. No. 207575, 763 SCRA 88, 94, July 15, 2015.

observe these periods would be cause for the dismissal of the judicial claim. But consider—if there is inaction on the part of the Commissioner to act within the 90-day period, and the taxpayer is forced to file a petition for review before the CTA, the taxpayer is left at a disadvantage for he or she cannot perfect an intelligent appeal before the CTA. As compared with an express denial by the Commissioner, when there is inaction, the taxpayer is left to speculate on the factual and legal basis underpinning why the administrative claim was "deemed denied."

It may be argued that when a taxpayer files a judicial claim, trial *de novo* is conducted before the CTA, meaning the parties are required to present proof on every minute aspect of their case.[138] Even if the Commissioner fails to act on the administrative claim for refund of excess and unutilized input tax, the taxpayer is still required to present evidence anew before the CTA. Be that as it may, the point remains that without affording the taxpayer the cardinal right of being informed in writing of the facts and the law supporting the denial of the claim, there is a violation of administrative due process on the part of the Commissioner. Even if the law provides that inaction of the Commissioner is a cause for the taxpayer to file his or her appeal before the CTA, such provision does not excuse the Commissioner from complying with the requirements of administrative due process. Such violation of due process is one that directly falls under the Arbitrariness Test.

Consider two taxpayers who are both claiming refunds of excess and unutilized input VAT for being exporters of goods. Companies A and B filed their administrative claims within the two-year period. The Commissioner denied the refund claim of Company A within 90 days from submission of official receipts, invoices, and supporting documents. Thereafter, Company A filed a petition for review before the CTA questioning the denial of the Commissioner and seeking relief from the court to grant the refund. In this case, Company A's pleadings would be able to substantially refute the factual and legal bases that supported the Commissioner's decision to deny the claim. In contrast, the Commissioner failed to act on Company B's refund claim within the 90-day period. The latter then filed a petition for review before the CTA. The difference lies in that in filing its appeal, Company B was left guessing as to why the Commissioner failed to act on its claim and is unable to create a more intelligent appeal like in Company A's pleadings.[139]

---

[138] Comm'r of Internal Revenue v. Manila Mining Corp., G.R. No. 153204, 468 SCRA 571, 588–89, Aug. 31, 2005.

[139] The appeal pertained here is a petition for review analogous to that filed under Rule 43 of the Rules of Court. *See* Rep. Act No. 1125 (1954), *amended by* Rep. Act No. 9282 (2004), § 11. *See also* A.M. No. 05-11-07-CTA (2005), rule 8, § 4.

Section 112(C) of the Tax Code likewise supports the view that there is arbitrariness when the Commissioner, his or her duly authorized representative, or any authorized BIR official fails to act on a claim for refund of excess and unutilized input tax within the 90-day period. Said Section provides that "failure on the part of any official, agent, or employee of the BIR to act on the application within the ninety (90)-day period shall be punishable under Section 269 of [the Tax] Code." This provision affirms the view that the 90-day period within which the BIR must act on the refund claim is mandatory in nature, and failure to comply with such period is a cause for the filing a criminal action against the BIR official or employee concerned. The law thus presumes that all refund claims should be acted upon within the 90-day period, and failure to comply therewith is an indication of an irregular or arbitrary act on the part of the BIR official or employee concerned.

Jurisprudence has likewise provided for instances when arbitrariness was present and necessitated the imposition of interest. These cases may be used as indicators of arbitrariness. In *Prieto*, the Court ruled that the then-Collector of Internal Revenue "had no reason to insist [o]n collecting the inheritance tax,"[140] thus interest was imposed. In *Commissioner v. Asturias Sugar Central, Inc.*,[141] the Court upheld the imposition of interest on Asturias Sugar Central's claim for refund because the Commissioner "acted arbitrarily in rejecting respondent's claim[.] [...] In other words, the assessment complained of is clearly unjustified, and, accordingly, the case at bar falls within the purview, not of the case of St. Paul's Hospital of Iloilo, but of the Carcar case."[142] In *Banco de Oro*, the Court ordered the payment of interest on the amount of PHP 4.966 billion, representing the 20% withholding tax on "PEACe" Bonds, since the Bureau of the Treasury's unjustified refusal to release the funds in escrow despite the order of the Supreme Court constituted arbitrariness.[143] These cases provide, at the very least, badges or examples that may be used by the courts in approximating whether an act falls under the Arbitrariness Test.

However, if it is the taxpayer who acted arbitrarily, such that he or she "acted negligently or in bad faith, or with willful oppression,"[144] the Court should not impose interest on the tax refund since Section 227 of the Tax Code provides that no "damages" shall be paid or reimbursed to the taxpayer in such cases. This would also disincentivize taxpayers who knowingly overpay taxes in the hope of securing a refund on which interest may be

---

[140] *Prieto*, 3 SCRA 101, 104.

[141] G.R. No. 15013, 3 SCRA 727, Dec. 28, 1961.

[142] *Id.* at 729.

[143] *Banco de Oro*, 800 SCRA 392, 463–65.

[144] TAX CODE, § 227.

imposed and which may accumulate over long periods of time—computed from the filing of the administrative claim. The intention of the taxpayer, whether or not he or she acted in good faith in filing the claim, may thus be a defense raised by the Commissioner, and the subject of judicial scrutiny in the same refund case. If there is arbitrariness in the actions of both the BIR and the taxpayer, such that the BIR acted arbitrarily in collecting the tax and the taxpayer was in bad faith in filing the refund claim, then no interest should be imposed in consideration of the *in pari delicto* principle.[145]

The determination of arbitrariness in the collection of tax is a judicial function that is exercised to balance the competing interests of both the taxpayer and the state. As Justice Isagani Cruz, one of the most eloquent jurists to have ever walked the halls of the Supreme Court, said: "Taxes are the lifeblood of the government and so should be collected without unnecessary hindrance. On the other hand, such collection should be made in accordance with law as any *arbitrariness* will negate the very reason for government itself. It is therefore necessary to reconcile the apparently conflicting interests of the authorities and the taxpayers so that the real purpose of taxation, which is the promotion of the common good, may be achieved."[146]

2. Proposed Guidelines

In view of the foregoing discussion, it is proposed that the Supreme Court, sitting *en banc*, reexamine the reasonableness and applicability of the No Statutory Authority Test since there is, as shown in this Paper, ample statutory authority allowing for the imposition of interest in tax refund cases. With regard to the Arbitrariness Test, which remains an important screening mechanism to determine whether interest may be imposed, the following guidelines are proposed:

For recovery of tax erroneously or illegally collected—

(1) Tax refunds of this type are considered as *solutio indebiti;*

---

[145] Though jurisprudence has exhibited that the principle of *in pari delicto* has been limited to tax assessments, specifically on the issue of the validity of waivers on the prescriptive period to assess, there is nothing that compels the courts not to apply it in tax refunds, since the principle is primarily rooted on equitable considerations. *See* Comm'r of Internal Revenue v. Next Mobile, Inc., G.R. No. 212825, 776 SCRA 343, 357, Dec. 7, 2015. ("*In pari delicto* connotes that the two parties to a controversy are equally culpable or guilty and they shall have no action against each other.")

[146] Comm'r of Internal Revenue v. Algue, Inc., G.R. No. 28896, 158 SCRA 9, 11, Feb. 17, 1988. (Emphasis supplied.)a

(2) Interest is imposable in accordance with Article 2159 of the Civil Code;
(3) Interest is imposable when there is arbitrariness present in the collection of the tax;
(4) Applying the guidelines in *Lara's Gifts*, interest may be imposed at the discretion of the court at the prevailing legal interest prescribed by the BSP, pursuant to Articles 2210 and 2011 of the Civil Code;
(5) Interest shall begin to run from the time the claim is made extrajudicially or judicially, i.e., upon the filing of the administrative claim which always precedes the judicial claim, until full payment of the tax refund; and
(6) No interest shall be imposed if the taxpayer-claimant acted negligently, in bad faith, or with willful oppression in accordance with Section 227 of the Tax Code.

For refund of excess and unutilized input tax—

(1) Interest in the concept of actual or compensatory damages may be imposed at the discretion of the court;
(2) Interest is imposable only when there is arbitrariness present in the collection of the tax, including but not limited to the following instances:
    (a) When the Commissioner fails to state in writing the factual and/or legal bases for the denial of the refund claim; or
    (b) When the Commissioner, his or her duly authorized representative, or any authorized BIR official, agent, or employee fails to act on the refund claim of the taxpayer within the 90-day period provided in Section 112(C) of the Tax Code, without prejudice to the criminal liability of the BIR official or employee concerned.
(3) Applying the guidelines in *Lara's Gifts*, interest may be imposed at the discretion of the court at the prevailing legal interest prescribed by the BSP, pursuant to Articles 2210 and 2011 of the Civil Code;
(4) Interest shall begin to run from the time the claim is made extrajudicially or judicially, i.e., upon the filing of the administrative claim which always precedes the judicial claim, until full payment of the tax refund; and
(5) No interest shall be imposed if the taxpayer-claimant acted negligently, in bad faith, or with willful oppression in accordance with Section 227 of the Tax Code.

C. Application

To better illustrate the proposed guidelines, the following examples are provided:

Example 1: Suppose Corporation A filed its annual income tax return (ITR) for calendar year 2020 on April 15, 2021. In its annual ITR, it was shown that Corporation A had excess payments of the quarterly tax due such that it has overpaid its annual income tax for the period, and it selected the refund option instead of the carry-over option. On April 15, 2022, Corporation A filed a claim before the Commissioner for recovery of tax erroneously or illegally collected. The Commissioner failed to act on the refund claim, and on April 14, 2023, before the lapse of the two-year prescriptive period, Corporation A filed a petition for review before the CTA. The CTA in division held that Corporation A was entitled to the refund, and it also found that the Commissioner acted arbitrarily in the collection of the tax when the income of Corporation A was exempted by law, as confirmed by a BIR ruling, and that the Commissioner failed to promptly act on the refund claim there being clear legal basis therefor. This was affirmed by the CTA *en banc*. The Supreme Court ruled that Corporation A was entitled to the refund and that the Commissioner acted arbitrarily. Thus, interest is imposable at the legal rate of 6% from the time of the filing of the administrative claim on April 15, 2022 until full payment.

Example 2: Suppose Corporation B is an actual exporter of goods to foreign buyers. In its quarterly VAT returns for the first to fourth quarters of calendar year 2020, Corporation B claimed excess and unutilized input tax for the said period. Thereafter, Corporation B filed an administrative claim for refund covering the first to fourth quarters of calendar year 2020 on June 30, 2021, attaching therewith all official receipts, invoices, and other supporting documents. The Commissioner failed to act on the refund claim within the 90-day period. Upon the lapse of that period, or on September 30, 2020, Corporation B filed an appeal. The CTA in division found merit in the claim of Corporation B and ordered the Commissioner to grant the refund. The CTA *en banc*, upon appeal of the Commissioner, affirmed the decision of the CTA in division. Then, the Supreme Court ruled that the CTA *en banc* was correct in affirming the CTA in division. Thus, interest at the legal rate of 6% is imposable because the failure of the Commissioner to act within the prescribed period is considered arbitrary. Interest at the legal rate of 6% shall run from the date of the filing of the administrative claim on June 30, 2021 until full payment.

Example 3: Suppose Corporation C sells goods to an entity registered in an ECOZONE. In its quarterly VAT returns for the first to fourth quarters of calendar year 2020, Corporation C claimed excess and unutilized input tax for the said period. Corporation C then filed an administrative claim covering the first to fourth quarters of calendar year 2020 on June 30, 2021, with attached official receipts, invoices, and other documents in support of the claim. The Commissioner denied the claim on August 30, 2021, but no factual and legal bases were provided in the decision. Corporation C filed an appeal with the CTA on September 15, 2021. The CTA in division found merit in the petition and ordered the Commissioner to grant the refund. The CTA *en banc* affirmed the decision of the CTA in division. Ultimately, the Supreme Court ruled that the CTA *en banc* was correct. Thus, interest at the legal rate of 6% is imposable because the failure of the Commissioner to provide the factual and legal bases of the denial was in violation of Section 112(C) of the Tax Code and Corporation C's right to administrative due process. Interest is to run from the date of the filing of the administrative claim on June 30, 2021 until full payment.

CONCLUSION

"A fool and his money are soon parted. It takes creative tax laws for the rest."[147] For so long, taxpayers have been at a disadvantage when it comes to tax refund claims. The prevailing law makes it hard for a taxpayer to claim a refund—the *onus probandi* lies with the taxpayer and doubts are construed strictly against him or her[148]—but there is no indemnity when the government itself made the error in not granting what is legally due the taxpayer. The state of the law is exacerbated by the prevailing attitude of the revenue agency, which tends to conveniently deny administrative claims or sit on them, since the taxpayer usually has another remedy available through the courts.[149] Even the Supreme Court has taken judicial notice of the taxpayers' generally negative perception towards the BIR,[150] especially the lethargic way the latter acts on taxpayers' refund claims. It has stated:

---

[147] Cohen v. United States, 578 F.3d 1 (D.C. Cir. 2009).

[148] Accenture, Inc. v. Comm'r of Internal Revenue, G.R. No. 190102, 676 SCRA 325, 345, July 11, 2012.

[149] But this has been mitigated when TRAIN provided for criminal liability when there is failure to act on the refund claim within the 90-day prescribed period. *See* TAX CODE, §§ 112(C), 269.

[150] Philex Mining Corp. v. Comm'r of Internal Revenue, G.R. No. 125704, 294 SCRA 687, 700, Aug. 28, 1998.

> In no uncertain terms must we stress that every public employee or servant must strive to render service to the people with utmost diligence and efficiency. Insolence and delay have no place in government service. The BIR, being the government collecting arm, must and should do no less. It simply cannot be apathetic and laggard in rendering service to the taxpayer if it wishes to remain true to its mission of hastening the country's development.[151]

As CTA Presiding Justice Roman Del Rosario stated in a *ponencia* before the Tax Court: "[a]ny unreasonable delay in the payment of refund to the taxpayer, sans any adverse consequence to the government, should no longer be countenanced[.]"[152] The imposition of interest on tax refund claims serves this purpose in several ways. *First*, it is an incentive on the part of the BIR to act on claims expeditiously, since failure to act within the statutory period shall be considered arbitrary. *Second*, it will serve to compensate the taxpayer for the damages caused by the BIR. *Finally*, it will ensure that the BIR observes the requirements of procedural due process in dealing with taxpayers. Importantly, the Arbitrariness Test remains the crucial screening mechanism to determine whether interest is to be imposed. Sound judicial discretion continues to be an important ingredient in this endeavor.

Ultimately, the disquisitions in this Note remain recommendations, unless and until the Supreme Court, sitting *en banc*, accepts the invitation to reexamine the current rules on the imposition of interest in tax refund cases. Indeed, the Supreme Court remains at the apex of the Philippine judicial system, and whose interpretation of "what the law is"[153] is final and binding. It is merely hoped that the Court accepts the challenge for the benefit of both the Government and Filipino taxpayer.

- o0o -

---

[151] *Id.*

[152] South Luzon Tollway Corp. v. Comm'r of Internal Revenue, CTA Case No. 9272 (Ct. of Tax Appeals July 27, 2018).

[153] Marbury v. Madison, 5 U.S. 137 (1803). "It is emphatically the duty of the Judicial Department to say what the law is."