SURVEY OF THE 1960 DECISIONS ON TAXATION LAW

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The year 1960 saw no significant change in the law of taxation—whether by statute or by judicial decision. The cases included in this survey are mostly either direct applications of a provision of the law or reaffirmation of principles laid down in cases previously decided by our Supreme Court.

I. INCOME TAX—

1. *Situs of income*—

In the case of *Collector of Internal Revenue v. Anglo California National Bank*,[1] the respondent, a foreign corporation, sold shares of stock of the Pampanga Sugar Mills to the Pasumil Planters Inc., a domestic corporation. The sale took place in San Francisco, California, where payment was made. The Collector of Internal Revenue attempted to levy a special gains tax, but the Court of Tax Appeals denied its right to do so on the ground that this was income derived by a foreign corporation from sources without the Philippines and thus not taxable as income under our law. In upholding the Court of Tax Appeals ruling, our Supreme Court stated that since under our law, a foreign corporation's income is taxable only when it is derived from sources within the Philippines, the income from the sale in question is not taxable here. The Court distinguished the situs of the shares of stock as personal property, and the situs of the income derived from the sale of such shares. The place of the sale is also the place of the source of income. And in ascertaining the place of the sale, the determination of when and where title to property passes from the seller to the buyer is decisive.[2] Hence, since the sale in question was perfected and consummated in California, the title to the shares passed from vendor to vendee at said place.

2. *Deductible items*—

Among the items deductible from gross income, in the determination of the net taxable income, is interest on indebtedness. Under the law, in order that such interest may be deductible, three things must be shown: (1) that there be an indebtedness, (2) that there should be interest upon such indebtedness, and (3) that what

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[1] G.R. No. L-12476, January 29, 1960.

[2] This, according to the Court, is the prevailing view, citing American authorities.

is claimed as interest deduction should have been paid or assessed within the year. In the case of *Commissioner of Internal Revenue v. Consuelo Vda. de Prieto*,[3] the question arose as to whether interest paid on delinquent taxes is deductible. In upholding the contention of the taxpayer, the Supreme Court defined the term "indebtedness" as an unconditional and legally enforceable obligation for the payment of money.[4] Within the meaning of this definition, it is apparent that a tax may be considered as an indebtedness. Thus, where a taxpayer pays interest due to late payment of a tax, although such interest is not deductible as a *tax* under Section 30(c) of the Tax Code,[5] it is deductible from the gross income as an *interest on indebtedness* under Section 30(b), provided that the interest is paid within the year it is sought to be deducted.

In the case of *Visayan Cebu Terminal Co. Inc. v. Collector of Internal Revenue*,[6] the respondent collector refused to allow a deduction for representation expenses because there was no documentary proof thereof. The Supreme Court held however that such deduction may be allowed in such amount as evidence, other than documentary, may prove. Thus, the trial court may make a comparison of the gross income and representation expenses of previous and subsequent years, with the gross income and the alleged representation expenses for the year in question, and allow a deduction accordingly.

II. BUSINESS TAXES—

1. *Sales Tax*—

Who is liable to pay the sales tax? Ordinarily, it is the seller, although such tax is charged to the purchaser by adding its amount to the price of the thing sold. However, where the amount of the tax is discounted from the purchase price, it may logically be inferred that the buyer takes upon himself the responsibility of paying the sales tax directly or assuming liability therefor to the Government. He may therefore be made to pay the tax. This was the ruling laid down by the Court in the case of *Collector of Internal Revenue v. Pio Barretto & Sons Inc.*[7]

The buyer is also liable for the tax where he is an importer of the thing sold. Where the things bought are acquired for his own

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[3] G.R. No. L-13912, Sept. 30, 1960.
[4] Court cited Mertens' Law of Federal Income Taxation, Vol. 4, p. 542.
[5] According to Sec. 80 of the Income Tax Regulations, "Taxes mean taxes proper and no deductions should be allowed for amounts representing interest, surcharge, or penalties incident to delinquency." This provision should not, according to the Court, be understood to preclude a deduction as "interest on indebtedness" under Section 30(b) of the Tax Code. Otherwise, the revenue regulations would be void because they would be inconsistent with the express provision of the Code in Sec. 30(b).
[6] G.R. No. L-12798, May 30, 1960.
[7] G.R. No. L-11805, May 31, 1960.

personal use, the importer is liable for compensating taxes, but where he imports them for mercantile purposes, he is liable for percentage or sales taxes. In the case of *Collector of Internal Revenue v. Cojuangco*,[8] Fernando Villabrille was awarded the bid for the purchase of some surplus properties at a U.S. Naval Base. As he did not have sufficient capital, he requested Cojuangco to provide the balance, which the latter did. Villabrille failed to pay all of the percentage tax on the sale, and the Collector assessed the deficiency against Cojuangco. After making it clear that percentage taxes are due on the sale because a purchaser from the Surplus Property Commission is an importer within the meaning of our Tax Code, the Supreme Court held that only Villabrille could be held liable on the tax because he was the buyer and importer of the goods. Cojuangco was merely a "contributor to the joint account enterprise," and the business remained exclusively Villabrille's.[9] As to the Collector's contention that agreements such as that between Villabrille and Cojuangco could be used to defraud the government of taxes, the Court stated that since the evidence showed no fraud, the desire to forestall future deceit does not justify the imposition of a tax on the wrong person.

2. *Fixed taxes*—

a. *On stevedoring business*—

In *Collector of Internal Revenue v. Bohol United Workers Inc.*,[10] the Collector collected a stevedore's fixed tax on the corporation on the ground that it was engaged in the business of stevedoring. To support his right to levy the tax, the Collector cited the following facts: Membership with the corporation is a condition precedent for employment of a laborer at the Tagbilaran port; it is the corporation which finds employment for its members and recommends to shippers or shipowners, who should be allowed to work at such port: no laborer can be dismissed without the approval of the corporation; in case of failure of shippers to pay the laborer-members for the handling charges, collection thereof is made with the aid of the

[8] G.R. No. L-13255, Sept. 29, 1960.

[9] Similarly, in Collector of Internal Rev. v. Alfonso Favis *et al.* (G.R. No. L-11551, May 30, 1960), the respondent was the buyer of a car from a tax exempt person. The Collector assessed the sales tax against the Favis Car Exchange on the theory that the real buyer was the latter and that the buyer was merely its dummy. The Supreme Court upheld the Court of Tax Appeals decision dismissing the case against the Favis Car Exchange because there was no evidence to show that it was the real buyer. Hence, it could not be held liable for the tax.

In Collector of Int. Rev. v. Cantilan Lumber Co. (G.R. No. L-14393, Oct. 31, 1960), the Collector demanded the compensating tax from a certain partnership for some equipment received by it from the U.S. Gov't. The partnership was later dissolved and Kellog bought most of the assets and liabilities of the partnership, including the equipment in question. Subsequently, Kellog sold all these properties to the Cantilan Lumber Co., a newly organized corporation of which Kellog was one of the principal stockholders and general manager. Said corporation refused to pay the compensating tax but the Supreme Court held that it was the one liable for the tax because it had acquired all the assets and liabilities of the partnership with the knowledge of the existing tax liability.

[10] G.R. No. L-12876, May 26, 1960.

corporation's legal counsel. In denying to the Collector the right to collect the tax, the Supreme Court held that these acts are legitimate functions of a labor union and that the defendant corporation merely serves as a labor organization to protect its members and cannot be said to be engaged in the stevedoring business.

b. *On real estate brokers—*

A broker engaged in the sale of real estate is not limited to bringing vendor and vendee together and arranging the terms and conditions of a sale of real estate. As sales of real estate must be in writing, the preparation of the documents is part of the functions of the broker. In the case of *J. M. Tuason & Co. Inc. v. Collector of Internal Revenue*,[11] the petitioner had agreed with the owners of several parcels of residential land to subdivide the lots and sell them for said owners in consideration of an "administration fee" to be paid by the owner and a certain percentage of the sales as commission. As part of its job, the petitioner was to prepare all documentation and papers in relation to sales of the subdivided lots. Upon receipt of the fee and commission, the Collector assessed a brokerage tax on the amount received as "administration fee." Petitioner claimed however that the tax is not due because the fee was paid for subdividing the lots and not for the sale thereof, and that the acts are not acts of brokerage. The Supreme Court however held that the tax was properly assessed pointing out that the only duty imposed on the petitioner which may be conceded to be distinct and separate from those of a broker is that of subdividing the land into lots and laying out the streets, parks and playgrounds, and constructing the streets, sewage systems and the like. All the others, such as recommending sales prices of lots, signing contracts of sale or lease, or releases of mortgage, collecting sales prices or other accounts due the owner, organizing offices and personnel to attend to the work relating to all of these are all necessary parts of the work of a real estate broker as defined by law.[12] The Court therefore concluded that since the contract of the parties was a single indivisible one because of indivisibility of consideration, for the reason that the parties fixed a so-called administration fee for developing the subdivision and for executing all necessary documentation and collection for the consummation of the sales, without possibility of determining the fees for each of the distinct prestations, the assessment must be upheld.

[11] G.R. No. L-11530, June 30, 1960.
[12] See Section 194(s), Nat'l. Int. Rev. Code.

III. ESTATE AND INHERITANCE TAXES—

In the case of *Melecio Domingo v. Judge Moscoso & Simeona Price*,[13] the Collector assessed the estate and inheritance tax on the estate of the deceased Walter Price and filed a claim in the intestate proceedings. No copy of the claim was furnished the administratrix, who was ordered by the Court to pay said tax. Six months later, when the Collector asked for the execution of the order to pay the tax, the administratrix opposed on the ground that the order was void because no copy of the claim was given to her. The Supreme Court upheld the order of payment stating that the failure to serve a copy of the claim is at most a legal error corrigible on appeal, and has no effect of depriving the court of jurisdiction over such claim. The Supreme Court reiterated the rule laid down in *Pineda v. Court of First Instance of Tayabas* [14] that claims for taxes due and assessed after the death of the decedent need not be presented in the regular form of claims in the estate or intestate proceedings. There is no need therefore, according to the Court, to furnish the administratrix with a copy thereof. Payment may therefore be validly ordered by the Court. Furthermore, the Court observed that it was too late to raise the question since the order of payment had already become final and executory, since more than six months had already expired.

IV. MISCELLANEOUS TAXES—

1. *Specific Tax*—

Specific taxes under section 124 of the Tax Code, are paid by the manufacturer, producer, owner or person having possession of the thing subject to the tax. In *Commissioner of Internal Revenue v. Central Azucarera Don Pedro*,[15] the evidence showed that the respondent corporation was manufacturing denatured alcohol which it sold to Pacific Industrial Manufacturing Co., which in turn used the same in the manufacture of rubbing alcohol compound. The petitioner levied a specific tax on the respondent under section 135 of the Tax Code, which imposes the tax on distilled spirits. The Supreme Court however flatly denied the power of the Commissioner to levy the tax on the respondent, holding that it is quite clear that it was the Pacific Industrial Manufacturing, and not the respondent, which was the manufacturer, producer and owner of the rubbing alcohol. It follows therefore that it, and not the respondent, is the party liable for the payment of the specific tax.

[13] G.R. No. L-14674, Jan. 30, 1960.
[14] 52 Phil. 803.
[15] G.R. No. L-14015, May 31, 1960.

2. *Amusement tax*—

The amusement tax is levied on the proprietor, lessee or operator of the place of amusement. In the case of *Silverio Blaquera v. Estefania Vda. de Aldaba and Court of Tax Appeals*,[16] the Supreme Court defined these terms as follows:

> "Proprietor is one who has the legal right of exclusive title to anything, whether in possession or not; an owner, sometimes, especially in statutory construction, in a wider sense, a person having interest less than absolute and exclusive right, as the usufruct, present control and use of property. (Vol. II Merriam-Webster 2d ed., p. 1986)
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> "An operator—(1) In general, one who or that which operates; as (a) one who produces an effect or does something; an agent; (b) one who does appropriate practical operations, as in business, art, or science; a professional or official performer of such work."

The evidence in the case showed that the defendant Aldaba was neither a proprietor nor an operator, but merely the "financier and capitalist" of the stage presentation.[17] The Supreme Court therefore upheld the Court of Appeals decision absolving the defendant from the amusement tax on the ground that the tax is imposed only on the proprietor, operator or lessee and not on any person to whom the gross receipts are destined and eventually paid.[18]

The tax collected from the operator, proprietor or lessee is levied on the gross receipts. In the case of cockpits, cabarets and night clubs the term "gross receipts" embraces all receipts of such proprietor, operator or lessee, irrespective of whether or not any amount is charged or paid for admission.[19] In the case of *Sy Chuico v. Collector of Internal Revenue*,[20] the Supreme Court applied this provision and held that the amount paid by a customer of a cabaret as dance fee is included within the gross receipts of the cabaret operator although such amount ultimately goes to the "bailarinas." And this is true even if an admission fee has been paid. According to the Court, this interpretation can be gleamed from the very terminology of the law wherein in "referring to the gross receipts the operation of the cabaret may realize it includes mainly all receipts 'irrespective of whether or not any amount is charged or paid for admission.' The law undoubtedly mainly contemplates to include the fees that may be paid by the customer for the privilege of dancing for it considers as incidental what may be paid by the customer as admission fee. In other words, the law in effect considers the amount charged

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[16] G.R. No. L-10534, March 30, 1960.

[17] This case involved the presentation of the opera "Madame Butterfly". At the time of its presentation, an opera was not exempt from the payment of any amusement tax on the receipts therefrom. Under Rep. Act 722, which took effect on June 6, 1952, subsequent to the presentation in question, an opera is exempt from the amusement tax.

[18] The Court cited Wong & Lee v. Collector of Internal Rev., G.R. No. L-10155, August 5, 1958.

[19] Section 250, National Internal Revenue Code.

[20] G.R. No. L-13387, March 28, 1960

against the customers for dancing with the 'bailarinas' as the main gross receipts of the cabaret, the admission fee thereto being merely incidental."

The above principle does not however apply in a case where any part of the gross receipts has been specially earmarked by law or regulation for some person other than the proprietor. In the case of *Commissioner of Internal Revenue v. Manila Jockey Club*,[21] the Commissioner of Internal Revenue levied the amusement tax on the gross receipts of the Manila Jockey Club, including the amount which the club paid to the Board on Races and the amount distributed as prizes for the owners of winning horses and bonuses for Jockeys. Republic Act 309 and Executive Order 320 expressly provide that ½% of the wager funds received by the Club was to go to the Board on Races and 5% to the prizes for winning horses and bonuses for jockeys. The Supreme Court, in affirming the Court of Appeals decision, denied the Commissioner the power to levy the amusement tax on the two latter amounts. With respect to the ½% which goes to the Board on Races, the Court observed that double taxation would result, said Board being a government institution, and that double taxation should be avoided unless the statute admits of no other interpretation. Since the law itself expressly directed the Manila Jockey Club to dispose of said amount in the manner that it did, and since said amounts never belonged to the Club, the 5½% of the wager funds should be excluded from gross receipts subject to the tax.[22]

3. *Forest charges*—

According to the Report of the Tax Commission, "forest charges are to be distinguished from taxes. They are strictly speaking, the price which the Government charges for the privilege granted to concessionaires to exploit the public domain, rather than a tax imposed to support the general services of the government. Since under the Constitution all timber lands in the public domain belong to the State, sound public policy demands that they be conserved or wisely exploited in order that the patrimony of the nation may not be impaired." [23] Therefore, forest charges are to be considered as internal revenue taxes only in the sense that they are to be collected by the Collector of Internal Revenue Code.[24]

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[21] G.R. Nos. L-13890 and L-13857, June 30, 1960.

[22] On the same principle, the Supreme Court in the same case denied the authority to tax the P10 contribution collected by the Manila Jockey Club from the horse owner to form a common fund which added to the above-mentioned 5% participation of the owners of the winning horses. The Club itself contributed also P10. The Court considered this contribution as a trust fund, and not as a part of "gross receipts", since they never belonged to the Club.

[23] Report of the Tax Commission, p. 36, Vol. 1, quoted in Collector of Internal Revenue v. Pio Barretto Sons, Inc., G.R No. L-11805, May 31, 1960.

[24] Collector of Internal Revenue v. Pio Barretto Sons, Inc., see note 23.

In the case of the *Collector of Internal Revenue v. Pio Barretto, supra*, the Supreme Court reversed the Court of Tax Appeals decision exempting the buyer of logs from paying forest charges. It appeared that the respondent company bought logs from licencees without the required invoices,[25] and without the forest charges having been paid. It claimed that it is the licensee of forest products who is liable to pay said charges and not the bona fide buyer of logs. The Supreme Court pointed out that the buyer of logs is bound to know the law and regulations regarding the payment of forest charges and the invoicing, transporting and discharging of such forest products. Unless he has complied with these regulations, he cannot be considered a purchaser in good faith. The Court further observed that a contrary holding would "create unlimited opportunities for licensees and buyers to connive with each other and cheat the State of its lawful revenues. Whether from a practical point of view or from that of public policy, forest charges should be considered as a lien on timber, and licensees or possessors of forest products, whoever they may be, should be made to respond for the forest charges and surcharges fixed in the law, and a lien should be pronounced on said timber or other forest products not only when they are yet in the condition of unsawn logs, but also after the same had been sawed into lumber and disposed of. It is only by such practical construction of the regulations and by the enforcement of such a public policy that the public patrimony may be saved from spoliation and ruin."

4. *Tax on dealers*—

In *Cebu Portland Cement Co. v. City of Manila and City Treasurer of Manila*,[26] the plaintiff was a manufacturer of cement with two cement factories outside Manila. Its principal office and warehouse is in Manila from which it distributes and disposes of its manufactured cement to consumers. The defendant assessed and demanded the dealer's tax imposed by an ordinance of the City of Manila. In denying the right of the City to collect the tax, the Supreme Court distinguished between a dealer and a manufacturer. Citing its previous decisions, the Court stated that a manufacturer is excluded from the term "dealer" for the purposes of the imposition of a dealer's tax where it only deals on or sells its own products.[27] The sole exception to this rule is when the manufacturer carries on business of selling its own products at stores or warehouses apart from its place of manufacture.[28] But the Court held that the said exception would

[25] These are prescribed by section 11 of the Revised Internal Forestry Regulations No. 85 dated December 28, 1934.
[26] G.R. No. L-14229, July 26, 1960.
[27] The Court cited City of Manila v. Bugsuk Lumber Co., 53 O.G. 6111.
[28] The Court cited Manila Tobacco Assn. Inc. v. City of Manila, G.R. No. L-9549, Dec. 21, 1957.

apply only where the manufacturer engages in the selling of its products at its very stores or warehouses, but not where the manufacturer maintains the warehouses merely for storage purposes, and from where it makes deliveries of the goods when sold.[29]

Similarly, where a bakery sells the empty cloth bags of flour after using the flour, it does not thereby become a "dealer" in second-hand goods. A dealer is not one who buys to keep or makes to sell, but one who buys to sell again. The sale of empty flour bags in this case however, was merely incidental to the business of bakery, so that the dealer's tax cannot be imposed on said sale.[30]

V. ASSESSMENT AND COLLECTION—

1. *Keeping of records as basis of assessment*—

In order to facilitate the assessment and collection of internal revenue taxes, all persons who are required by law to pay the same must keep a journal and a ledger or their equivalents. However, where the gross quarterly receipts of the taxpayer do not exceed ₱5000, it is sufficient if he keeps a simplified set of bookkeeping records, provided the latter have been approved by the Secretary of Finance.[31] The question as to whether the Secretary of Finance has the power to grant permission to more than one person to print simplified records for sale to the public was raised in the case of *Felipe Ollada v. Sec. of Finance.*[32] In answering the question in the affirmative, the Supreme Court stated that for the purposes of the law, what is important is that the simplified records should contain the necessary data from which the taxes due may be ascertained. A person who has been granted permission to print such simplified records for sale to small-scale merchants, acquires said permission subject to the implied condition that the Secretary may at any time, change or repeal any of the regulations issued by him, as he may see fit. The authority to print does not carry with it an assurance of monopoly or guarantee of a ready market or vested property rights.

Once an assessment is made by the Collector of Internal Revenue based on the records of the taxpayer, the presumption is that the assessment is correct. The burden of proof is on the taxpayer to show the contrary.[33]

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[29] Court cited Central Azucarera Don Pedro v. City of Manila, G.R. No. L-7669, Sept. 29, 1955.
[30] Ah Nam v. City of Manila, G.R. No. L-15502, Oct. 25, 1960.
[31] See Sec. 334 National Internal Rev. Code
[32] G.R. No. L-15397, Oct. 31, 1960.
[33] Collector of Internal Rev. v. Bohol Land Trans. Co., G.R. Nos. L-13099 & 13462, April 29, 1960

2. *Jurisdiction of court over collection cases—*

Where the taxpayer disputes an assessment, he should do so within the period allowed by law by appealing the Collector's decision to the Court of Tax Appeals. But where he fails to dispute said assessment, and the latter thus becomes final, executory and demandable, the Government may collect the tax by an ordinary civil action not before the Court of Tax Appeals but before the proper Court of First Instance. This was the holding of the Supreme Court in the case of *Republic of the Philippines v. Enrique Magalona Jr.*,[34] where the court upheld the jurisdiction of the Court of First Instance in rendering judgment in favor of the Collector.[35] The Supreme Court also made the observation that a mere statement made by the delinquent taxpayer that he believes himself not liable for the taxes assessed against him is not a sufficient "dispute" of the assessment to bring the case within the exclusive jurisdiction of the Court of Tax Appeals. Such a statement is a mere expression of a belief and conviction personal to the taxpayer and not binding on the Collector.

3. *Prescription of the right to assess and collect—*

The right of the Government to collect taxes can be exercised only within a limited period of time prescribed by law. Just as the government is interested in the stability of its collections, so also are the taxpayers entitled to an assurance that they will not be subjected to further investigation for tax purposes after the expiration of a reasonable period of time.[36] The Supreme Court, in the case of *Republic of the Philippines v. Luiz Ablaza*,[37] further justifies this rule of prescription as follows:

> "The law prescribing a limitation of actions for the collection of the income tax is beneficial both to the Gooevrnment and to its citizens; to the Government because tax officers would be obliged to act promptly in the making of assessments, and to citizens because after the lapse of the period of prescription citizens would have a feeling of security against unscrupulous tax agents who will always find an excuse to inspect the books of taxpayers, not to determine the latter's real liability, but to take advantage of every opportunity to molest peaceful, law-abiding citizens. Without such a legal defense taxpayers would furthermore be under obligation to always keep their books and keep them open for inspection subject to harassment by unscrupulous tax agents. The law on prescription being a remedial measure should be interpreted in a way conducive

[34] G.R. No. L-15832, Sept. 30, 1960.
[35] The Supreme Court applied the same principle in the case of Republic of the Philippines v. Victoriano Medrano, G.R. No. L-15777, Oct. 22, 1960 and in Republic v. Court of Tax Appeals, G.R. No. L-15021, Sept. 30, 1960. In the latter case, liability was admitted by the filing of bond.
[36] Volume II, Report of the Tax Commission of the Philippines, pp. 321-322, cited in Republic of the Phil. v. Luis Ablaza, G.R. No. L-14519, July 26, 1960.
[37] See note 36

> to bringing about the beneficient purpose of affording protection to the taxpayer within the contemplation of the commission which recommended the approval of the law."

Having in mind these reasons, the Supreme Court held that although a letter asking for reinvestigation of the liability of the taxpayer would suspend the running of the prescriptive period, a mere request for a copy of the assessment cannot have the same effect.

As a general rule, the Collector's right to assess internal revenue taxes prescribes five years after the returns have been filed,[38] and any court action for the collection of the tax so assessed must be brought within five years from said assessment.[39] As to what is meant by "court action" or "judicial action" was explained by the Supreme Court in the case of *Collector of Internal Revenue v. Bohol Land Transportation*.[40] Citing the Court of Appeals decision, the Supreme Court said:

> " . . The judicial action contemplated may refer not only to the civil case instituted by the government to collect the tax but also to a case where the taxpayer takes the initiative to contest the validity of the assessment or collection of taxes by the Collector of Internal Revenue. The objective in both cases is the same—the validity and correctness of the determination and collection of the tax. Thus, a single claim filed by the collector of Internal Revenue against the estate of a deceased in a probate case has been recognized as tantamount to judicial collection of taxes. (Collector v. Haygood, 65 Phil. 520). On the other hand, in a claim for refund instituted against the Collector of Internal Revenue, the Supreme Court considered the taxpayer's suit for refund as sufficient judicial action for the collection of taxes on the part of the former. (See Phil. Sugar Estate Dev. Co. Inc. v. Posadas, 65 Phil. 216)

As to whether the defense of prescription can be impliedly waived by the taxpayer after the prescriptive period has elapsed was answered in the negative by the Supreme Court in the case of *Collector of Internal Revenue v. Cia. General de Tabacos de Filipinas et al.*[41] The Collector tried to collect the tax long after the prescriptive period had elapsed, but claimed that since the taxpayer, in answer to the assessment made by the Collector, had objected to the amounts assessed resulting in revised assessments, said communications from the taxpayer constituted a waiver of the defense of prescription. The Supreme Court however brushed aside this contention and denied the right of the Collector to collect stating that the alleged communications could not have the effect of waiving the defense of

[38] See Section 331, Natl. Int. Rev. Code.
[39] See Section 332(c) Natl. Int. Rev. Code
[40] G.R. Nos. L-13099 and L-13462, April 29, 1960.
[41] G.R. No. L-11151, July 30, 1959

prescription because they were exchanged long after the prescriptive period had expired.

But where the issue of prescription is not raised in the Court of Tax Appeals and is for the first time alleged before the Supreme Court, the taxpayer will be deemed as having waived said defense since to hold otherwise would be to deprive the Collector of his right to show the contrary, this matter being evidentiary in nature.[42]

The general prescriptive period of five years provided in sections 331 and 332 of the Tax Code does not apply to the collection of forest charges, because the latter are not strictly speaking internal revenue taxes.[43]

4. *Penalties* —

Where the taxpayer is guilty of fraud in his income tax returns, the Collector of Internal Revenue has authority to add a surcharge to the deficiency tax.[44] Although there may be no direct evidence of actual fraud, where the taxpayer has deliberately omitted in his books a sizable portion of his taxable income, such act of the taxpayer amounts to fraud and the Collector can rightfully impose a surcharge as penalty.[45]

But the penalties of interest or surcharge must be imposed by the lower court and where the latter's decision is silent as to these and the question of their being due was squarely raised by the pleadings, the said decision replaces the original assessment, and the execution of said judgment cannot include interest and surcharge. The remedy of the Collector in such a case is to appeal from the judgment in so far as it failed to provide for the payment of surcharge and interest. If he fails to do so and the decision becomes final, the Collector may not vary the terms thereof by including in his motion for execution the payment of surcharge and interest.[46]

VI. REMEDIES OF THE TAXPAYER —

1. *Claim for refund* —

Where an internal revenue tax has been erroneously collected or paid, the first step that the taxpayer should take is to claim for a refund of the same within two years after the payment of said tax. Failure to file said claim within the said period will bar any future demand for a refund, whether judicial or extra-judicial.[47]

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[42] Sy Chuico v. Collector of Int. Rev., *supra*.
[43] See previous discussion on this point.
[44] See Section 72, Nat'l. Int. Rev. Code.
[45] Sy Chuico v. Coll. of Int. Rev., *supra*.
[46] Coll. of Int. Rev. v. Blas Gutierrez, G.R. No. L-13819, May 25, 1960.
[47] See Section 309, Natl. Int Rev. Code.

The authority to compromise, credit or refund internal revenue taxes erroneously collected is vested by law exclusively on the Collector of Internal Revenue in order to assure that no improper compromise, credit or refund is made to the prejudice of the Government.[48] But where the action is one denying a request for refund, such action is well within the authority of the Deputy Collector of Internal Revenue and is final and binding, unless revoked by the Collector.[49]

Where the tax involved is not an internal revenue tax, the period within which a claim for refund may be made is not governed by the National Internal Revenue Code but by the ordinary rule of prescription found in the Civil Code, in the absence of any special provision to the contrary. Thus in the case of *Beiman Compania Incorporada v. Central Bank of the Philippines*,[50] where the exchange tax was paid under mistake, the Supreme Court held that since the basis of the action for refund is *solutio indebiti*, a quasi-contract, the period of prescription is six years as provided for by Article 1145(2) of the New Civil Code.[51]

In the case of *Antonio Rodriguez v. Blaquera*,[52] the Supreme Court reiterated the principle that an action in the nature of declaratory relief to determine the rights and obligations of a taxpayer under a tax statute is altogether improper as a step preparatory to a claim for refund. Such an action is explicitly prohibited by Act 3736 as amended by Rep. Act 55.[53]

2. *Appeal to Court of Tax Appeals* —

Under section 7 of Rep. Act 1125 creating the Court of Tax Appeals, the latter court has exclusive jurisdiction over decisions of the Collector of Internal Revenue in cases involving, among other things, disputed assessments and refund of internal revenue taxes. Therefore, as long as the primordial and immediate question involved in a case is the validity of tax assessment or the refund of taxes alleged to have been illegally collected, the Court of Tax Appeals has jurisdiction over the case, although the appeal might have

[48] Allison J. Gibbs v. Esther K. Gibbs, G.R. No. L-13453, Feb. 29, 1960.
[49] *Ibid.*
[50] G.R. No. L-15044, May 30, 1960 and July 14, 1960.
[51] The action here had prescribed since more than 6 years had elapsed from the payment of the tax and the claim for refund. The Court, in its first decision dated May 30, 1960 applied the period of 5 years under Article 1149 of the Civil Code, which sets down such period with respect to "all other actions where periods are not fixed in the law." A motion for reconsideration was filed by the taxpayer who claimed that since the obligation to refund the taxes is one created by law, the ten-year period and not the five-year period should apply under Art. 1144 of the Civil Code. The Court admitted that the five-year period under Article 1149 was not applicable to the case, but it refused to apply the ten-year period and instead held that the 6-year period applied since it involved payment under mistake, a quasi-contract, the period of prescription for which is governed by Article 1145(2).
[52] G.R. No. L-13941, Sept. 30, 1960.
[53] The Court cited National Dental Supply v. Meer, G.R. No. L-4183, Oct. 26, 1951.

the indirect effect of reviewing an action of the Secretary of Finance.[54]

Under section 11 of the same Republic Act, an appeal to the Court of Tax Appeals from a decision of the Collector of Internal Revenue should be made within 30 days from said decision, otherwise the decision or assessment of the Collector will become final and unappealable. This period of 30 days is jurisdictional and non-extendible.[55] And although a motion for reconsideration of a decision will suspend the period of appeal, a taxpayer cannot, by filing subsequent motions for reconsideration, after denial of the first motion, put off indefinitely and at his convenience the finality of a tax assessment. Such was the ruling of the Supreme Court in the case of *North Camarines Lumber Co. Inc. v. Collector of Internal Revenue*.[56] And the 30-day period should be counted from the date that a taxpayer receives the letter denying the first motion for reconsideration.[57] In this connection, however, our Supreme Court held in the case of *Collector of Internal Revenue v. Court of Tax Appeals*[58] that the rule against *pro forma* motions should not be very strictly applied in tax cases for the reason that the Rules of Court is only suppletory in character before the Court of Tax Appeals. Therefore, a *pro forma* motion for reconsideration filed before the Collector of Internal Revenue may effect a suspension of the period of appeal, specially in view of the fundamental principle that one must exhaust all administrative remedies before resorting to the courts.

Said section 11 of Rep. Act 1125 providing the 30-day period within which to appeal must however be construed together with Section 306 of the National Internal Revenue Code, providing a 2-year period for claiming refund of internal revenue taxes. A taxpayer who has paid the tax, whether under protest or not, and who is claiming a refund of the same, must comply with the requirements of both sections; that is, he must file a claim for refund with the Collector of Internal Revenue within 2 years from the date of his payment of the tax, as required by said Section 306 of the Tax Code, and appeal to the Court of the Tax Appeals within 30 days from receipt of the Collector's decision or ruling denying his claim for refund, as required by said Section 11 of Republic Act 1125. If however, the Collector takes time in deciding the claim,

[54] Lu Do & Lu Ym Corp. v. Central Bank of the Phil., G.R. No. L-13033, May 31, 1960; Commissioner of Int. Rev. v. Phil. Corn Products Inc., G.R. No. L-13701, May 31, 1960. See also Coll. of Int. Rev. v. Mariano Lacson, G.R. No. L-12945, April 29, 1960.

[55] Pangasinan Trans. Co. v. Blaquera, G.R. No. L-13101, April 29, 1960. Also Allison J. Gibbs v. Esther K. Gibbs, see note 48.

[56] G.R. No. L-12353, Sept. 30, 1960.

[57] Tomas B. Villamin v. Court of Tax Appeals & Coll. of Int. Rev., G.R. No. L-11536, Oct. 31, 1960.

[58] G.R. No. L-14902, Oct. 31, 1960.

and the period of two years is about to end, the suit or proceeding must be started in the Court of Tax Appeals before the end of the two-year period without awaiting the decision of the Collector. This is so because of the positive requirement of Section 306 and the doctrine that delay of the Collector in rendering a decision does not extend the peremptory period fixed by statute.[59]

VII. EXEMPTIONS —

The well-settled principle that a law granting tax exemption should be strictly construed against the taxpayer was applied by the Supreme Court in several cases. In the case of *Lu Do & Lu Ym Corporation v. Central Bank of the Philippines, supra,* the Supreme Court refused to exempt imported cotton bags from the compensating tax due from the petitioner who was employed in the manufacture and sale of corn starch. Although the petitioner had been granted exemption from said tax in its machinery and equipment used exclusively in the new and necessary industry, the Court pointed out that cotton bags are not "equipment" within the meaning of the exemption. Such word should be taken together with the term "machinery" and must therefore relate to furnishings necessary for the operation of the industry, and cannot include empty cotton bags used in the packing of the finished products.[60] Similarly, in *Philippine Racing Club Inc. v. Collector of Internal Revenue,*[61] the Supreme Court also denied petitioner's claim of exemption from income tax because the exemption granted to it by law [62] is limited to the municipal license fee imposed on any person or entity conducting a horse race and to the fixed tax imposed for each day on which races are run on the tracks.

Consistent with the same principle of strict interpretation of exemptions are the decisions of the Supreme Court in the cases of *Collector of Internal Revenue v. Mariano Lacson,*[63] and *Marcelo Steel Corp. v. Collector of Internal Revenue.*[64] In the first case, the taxpayer claimed exemption from forest charges on his lumber in view of the fact that he had been granted an exemption from the payment of *all* taxes in connection with the manufacture of veneer and plywood from Philippine wood. In denying the exemption claimed for,

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[59] Allison J. Gibbs v. Father K. Gibbs, see note 48. Court cited US v. Michel, 282 US 656; Kieler & Co. v. David, G.R. No. L-5163, April 22, 1953; College of Oral & Dental Surgery v. Court of Tax Appeals, G.R. No. L-10446, Jan. 28, 1958.

[60] Compare this with Collector of Int. Rev. v. Industrial Textile Co., G.R. No. L-10936, April 25, 1958, where the petitioner was engaged in a new and necessary industry of manufacturing jute bags and which industry was exempted from tax on all "articles, good or materials used exclusively in the new and necessary industry." The Supreme Court upheld its exemption from tax on the cement used for the construction of the building which would house its machinery and equipment for the production of jute bags. See Phil. Law Journal, Vol. XXXIV, No. 2, p. 295.

[61] G.R. No. L-12781, Aug. 31, 1960.

[62] Rep Act No. 29, sec. 3.

[63] G.R. No. L-12945, April 29, 1960.

[64] G.R. No. L-12401, Oct. 31, 1960.

the Supreme Court distinguished between forest charges and taxes,[65] and concluded that although logs and lumber are necessary in the manufacture of plywood, the *operation* of a forest concession is certainly not so. The lumber can be bought from other forest concessionaires, who would of course be liable for the forest charges.

In the second case, Marcelo Steel Corporation was engaged in the manufacturing of wire fences, nails and steel bars. For the manufacture of nails and steel bars, it was exempt from tax as a new and necessary industry. When the petitioner incurred losses in the manufacture of nails and steel bars, it sought to deduct such losses from its taxable industries. The Supreme Court denied its right to so deduct and stated that the law[66] merely exempts the new and necessary industry and cannot cover an already going concern, although they may be operated by only one corporation. Unlike the new and necessary industry, a taxable or non-exempt industry, being already a going concern, derives profits from its operation and deserves no subsidy from the Government. The Court also gave the reason for the exemption of new and necessary industries from taxes as follows:

> "The purpose or aim of Rep. Act 35 is to encourage the establishment or exploitation of new and necessary industries to promote the economic growth of the country. It is a form of subsidy granted by the government to courageous entrepeneurs staking their capital in an unknown venture. An entrepeneur engaging in a new and necessary industry faces uncertainty and assumes a risk bigger than one engaging in a venture already known and developed. He does not expect an immediate return on his investment. Usually loss is incurred rather than profit made. Therefore the law grants exemption to lighten the onerous financial burdens and reduce losses."

On the other hand, where the evidence shows that the taxpayer is clearly exempt from taxes, the Supreme Court will not hesitate to uphold the exemption. Thus, in the case of *Manila Polo Club v. Bibiano Meer*,[67] since the evidence clearly showed that the petitioner was merely a social club, not run for profit, it was free from the fixed and percentage taxes on the sale of food and drinks to its members made it bar and restaurant. That such sale is merely incidental to its objective as a social club is clearly shown by the fact that

[65] See discussion on "Forest Charges", *supra*.
[66] Republic Act No. 35.
[67] G.R. No. L-10854, Jan. 27, 1960.
[68] The Court explained this formula and stated that the club charged its patrons the cost of the drinks and food served, plus an amount sufficient merely to cover the expenses for the operation of the bar and restaurant.

it was made strictly on the "cost-plus-expenses" bases,[68] without any profit.[69]

VIII. CUSTOMS —

The provision of the Revised Administrative Code [70] which authorizes the forfeiture of merchandise imported contrary to law was again applied by the Supreme Court in several cases. In *Commissioner of Customs v. Seree Investment Co.*,[71] the Supreme Court held that Circular 44 of the Central Bank prohibiting importation of merchandise without a release certificate from said Bank, being issued under authority of law, has the effect of law and any merchandise imported contrary thereto is imported contrary to law, empowering therefore the Commissioner of Customs to seize and forfeit such merchandise.[72] In *Luz H. Coloma v. Commissioner of Customs & Court of Tax Appeals*,[73] the Supreme Court reiterated its ruling in *Commissioner v. Relunia*,[74] that all vessels whether private or government owned, including ships of the Philippine Navy, coming from a foreign port, with the possible exception of war vessel or vessels employed by any foreign government not engaged in the transportation of merchandise in the way of trade, are required to prepare and present a manifest to the customs authorities upon arrival at any Philippine port. Failure to do so would empower the Commissioner of Customs to forfeit the unmanifested merchandise.

As to whether Philippine pesos are "merchandise" within the meaning of the Customs Law as to empower the Commissioner of Customs to forfeit the same when illegally exported, was answered by the Supreme Court in the affirmative in the case of *Commissioner of Customs v. Caridad Capistrano*.[75] The Court stated that merchandise, when used with reference to importation or exportation, includes goods, wares, and in general anything that can be a subject of importation or exportation, and that money may certainly be a commodity and thus an object of trade.

IX. MUNICIPAL TAXATION —

In *City of Manila v. Arcadio Pallugna*,[76] the validity of an ordinance of the City of Manila exacting a license fee for the opera-

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[68] This case is similar to Collector of Int. Rev. v. Manila Lodge No. 761 et al., G.R. No. L-11176, June 29, 1959 and Coll. of Int. Rev. v. Sweeney, G.R. No. L-12178, Aug. 21, 1959. See Phil. Law Journal, Vol. XXXV, No. 2, p. 846 and footnote 24. See also Coll. of Int. Rev. v. St. Paul Hosp. of Iloilo, G.R. No. L-12127, May 25, 1959, Phil. Law Journal, Vol. XXXV, No. 2, p. 857.

[70] Sec. 1363(f)

[71] G.R. No. L-12007, May 16, 1960.

[72] To the same effect, see also Po Eng Trading v. Comm. of Customs, G.R. No. L-10508, Nov. 29, 1960

[73] G.R. No. L-14217, Nov. 29, 1960.

[74] G.R. No. L-11860, May 29, 1959. See Phil. Law Journal, Vol. XXXV, No 2, p. 858.

[75] G.R. No. L-11075, June 30, 1960.

[76] G.R. No. L-15305, Sept. 30, 1960.

tion of pinball machines was questioned. The Supreme Court held that it was an *ultra vires* ordinance, not because it was a tax measure, but because it sought to regulate device which are prohibited by law.

In *Antonio Heras v. City Treasurer of Quezon City*,[77] the Supreme Court held that under the charter of Quezon City, what has been voluntarily paid as taxes without protest cannot be recovered.[78]

[77] G.R. No. L-12565, Oct. 3, 1960.

[78] Sec. 63 of Rep. Act 537, Charter of Quezon City, enjoins all courts from entertaining any suit for recovery of taxes unless they have been paid under protest.