Significant Court of Tax Appeals Decisions
July 2018

A holding company is not subject to local business tax (LBT) on dividend income.

The Court ruled that the taxpayer is a holding company and not an investment company nor a bank and/or other financial institution as can be seen on its Articles of Incorporation (AOI). Its primary purpose does not show that any of its activities are covered by the BSP Manual akin to functions pertaining to a financial intermediary. As a holding company, it is not subject to LBT on dividend income. *(Metro Pacific Assets Holdings, Inc. v. Makati City, Case AC-184, July 2, 2018)*.

Absent any decision from the Commissioner of Customs (COC) in the seizure and forfeiture proceedings, the CTA did not acquire jurisdiction over the matter.

The taxpayer allegedly imported rice without import permits from the National Food Authority. Consequently, the Bureau of Customs (BOC) refused to release the rice shipments. After their seizure, taxpayer's rice shipments were subjected to forfeiture proceedings. The taxpayer filed a Consolidated Motion for Release Under Cash Bond. Pending resolution of the Motion, the taxpayer filed a petition for review with the CTA. The CTA ruled that it has no jurisdiction over the case absent any decision from the COC in the seizure and forfeiture proceedings over the subject rice shipments. *(The Bureau of Customs and the Commissioner of Customs v. Jade Bros Farm and Livestock, Inc., CTA Case EB 1566, July 4, 2018)*.

The CTA has jurisdiction to act on disputed assessment and not when the assessment has become final, executory and demandable for taxpayer's failure to file protest.

On September 19, 2013, the taxpayer received a FAN for alleged tax deficiency of around P500 Million. Counting 30 days from receipt thereof, petitioner had until October 19, 2013 within which to file its protest. However, instead of filing a protest, petitioner wrote a letter to the BIR on November 21, 2013 stating that it made a partial payment, inclusive of the 20% interest based on the FAN. It was only on February 17, 2014 that the taxpayer filed a letter requesting for reinvestigation of tax deficiency.

The court ruled that for failure to file a protest within the reglementary period, the assessment in question became final, executory, and demandable. The fact that an assessment has become final for failure of the taxpayer to file a protest within the reglementary period means that the validity or correctness of the assessment may no longer be questioned on appeal. Consequently, the CTA had no jurisdiction to entertain such case. *(Grand Plaza Hotel Corporation v. Commissioner of Internal Revenue, CTA Case No. 8992, July 4, 2018)*.

Deficiency income tax and VAT may not be assessed on the basis solely of under-declared purchases.

The sole basis of the assessment of deficiency income tax and VAT is the alleged under-declared purchases arising from the comparison of the amount of the taxpayer's purchases per Summary List of Purchases and the amount of its purchases per its VAT returns.

The court, in cancelling the assessment, ruled that income tax is assessed on income received from any property, activity or service. Such being the case, in the imposition or assessment of income tax, it must be clear that there was an income, and such income was received by the taxpayer, and not when there is an under-declaration of purchases. Moreover, it is important to note that, for income tax purposes, a taxpayer is free to deduct from its gross income a lesser amount, or not to claim any deduction at all. What is prohibited by the income tax law is to claim a deduction beyond the amount authorized therein. Thus, even when there is under-declaration of purchases, the same is not prohibited by law. Accordingly, mere reliance on the fact that there were under-declared purchases is not enough basis for the court to uphold respondent's assessment of the subject deficiency income tax.

As regards deficiency VAT, the court held that VAT can be imposed only when it is shown that the taxpayer received an amount of money or its equivalent from its sale, barter or exchange of goods or properties, or from sale or exchange of services, and not when there are under-declared purchases. In other words, the VAT is imposed when one sells, not when one purchases. *(Philippine Power MC Distribution, Inc., v. Commissioner of Internal Revenue, CTA Case No. 9263, July 6, 2018).*

Section 228 of the Tax Code does not apply to assessment for violation of other provisions of the Tax Code and tax rules and regulations.

Upon assessment, the taxpayer paid to the BIR miscellaneous penalties in the aggregate amount of ₱5,600,000.00 allegedly for the following violations: (a) no books; (b) no official receipts; (c) no back-end report; and (d) unaccounted point-of-sales machines, and subsequently claimed a refund.

A. In its claim for refund, the taxpayer argued that it was not afforded due process in accordance with the provisions of Section 228 of the Tax Code.

The court, in not upholding the taxpayer's contention, ruled that Section 228 of the Tax Code does not apply to assessment for violation of other provisions of the Tax Code and tax rules and regulations. The imposition of the said penalties was not a result of regular examination of internal revenue tax liabilities under Section 203 of the Tax Code but it was an outcome of the inspection of the taxpayer's compliance with the administrative provisions of the Tax Code, more particularly with regard to the keeping of books of accounts, official receipts and related financial records. Hence, Section 228 does not apply in the instant case.

Note: **In assessments issued by the BIR as a result of regular examination of the taxpayer's internal revenue tax liabilities and not just as an outcome of inspection of the taxpayer's compliance with the administrative provisions of the Tax Code, the BIR also would normally include findings on taxpayer's non-compliance with administrative compliance requirements, booking and invoicing requirements which would warrant the**

imposition of compromise penalties. In case these findings were stated in such assessments, would this decision of the CTA in *Frankfort* case still apply?
B. The taxpayer also argued that the BIR had no basis to impose and collect said penalties in such amount in the absence of a written offer from the taxpayer.

The court held that in the absence of a written offer from the taxpayer, the amount of compromise penalties to be imposed must be those stated in RMO 19-2007 (now RMO 07-2015). Under the said RMO, taxpayer's penalties amounted to only ₱150, 000.00. Hence, the CTA partially granted taxpayer's claim of refund in the amount of ₱5, 450,000.00. *(Frankfort, Inc. v. Commissioner of Internal Revenue, CTA Case No. 9363; July 10, 2018).*

Note: **This decision of the CTA in the *Frankfort* case departs from the court's previous rulings that in the absence of any proof that the taxpayer consented to a compromise penalty, the imposition of compromise penalty should not be allowed.**

To hold the taxpayer liable for percentage or amusement tax, there must be sufficient proof that it operates as a cabaret, night or day club.

For the taxpayer to be deemed a cabaret, or night and day club, it must be established that its operations involve dancing as the main business and customers patronize the place in order to dance either with their own partners or with professional hostesses engaged by petitioner for that purpose.

The evidence, however, showed that the business activities of the taxpayer do not fall within the scope or coverage of cabarets and/or night or day clubs, since there is no indication that its customers frequent its establishment to dance, either with their own partners, or with professional hostesses provided by the taxpayer. It has no dance floor, nor does it encourage its customers to dance. The evidence presented showed that the actual business activities of the taxpayer r are those of a restaurant, with the entertainment usually by the performances of live bands, which is merely incidental to its main business to encourage or attract customers with the end in view of promoting sales of food and drinks served in the restaurant. Moreover, no tickets are sold by petitioner to its customers to view the live band as it is but a part of the service to customers as they dine. ***[Hard Rock Café*** *(Makati City), Inc. v. Commissioner of Internal Revenue, CTA Case No. 9279, July 12, 2018].*

Note: **The Court did not adopt the definition of the terms cabarets, night and day clubs under RMC 18-2010 to include other places which offer similar pleasurable diversion entertainment and function such as videoke bars, karaoke bars, karaoke televisions, karaoke boxes and music lounges, for purposes of imposing amusement tax. RMC 18-2010 unilaterally changed and expanded or widened the scope or meaning of the terms cabarets, night and day clubs as defined under the Tax Code and in existing jurisprudence. When there is a conflict between administrative issuances and jurisprudence, it is the latter which shall prevail.**