Significant Court of Tax Appeals
September 2018

The buyer of services must be a non-resident foreign corporation doing business outside the Philippines to qualify under zero percent VAT.

In this case, the taxpayer claims that the services it rendered to its affiliates abroad are transactions subject to zero percent VAT. In the course of trial, it presented a certificate of non-registration of corporation from the Securities and Exchange Commission (SEC) and a service agreement. The Court held that these documents merely proved that the buyer is a non-resident foreign corporation.

To prove that the buyer is "a non-resident foreign corporation doing business outside the Philippines", the buyer entity must be supported by both (1) certificate of non-registration from SEC and (2) proof of incorporation in a foreign country and (3) that there is no other indication which would disqualify the buyer in being classified as a non-resident foreign corporation. *(Procter & Gamble Asia, PTE. LTD vs. CIR, CTA Case No. 7683, September 6, 2018).*

The three-year limitation period to assess applies also to withholding tax assessments.

The BIR believes that withholding tax assessments are not internal revenue taxes, but assessments issued for failure of the company to withhold the correct taxes. As such, the three-year limitation period to assess shall not apply. The Court ruled differently. It says that the withholding tax falls under the income tax and shall therefore be assessed within the period of three years. *(Thunderbird Pilipinas Hotels and Resorts, Inc. vs. CIR, CTA Case No. 8612, September 6, 2018).*

The issuance of a second LOA for regular audit does not repeal the first LOA issued under the VAT audit program.

Taxpayer contends that the first LOA was cancelled upon the issuance of the second LOA since the second LOA includes the tax type and tax period covered by the first LOA. The Court held that on situation wherein the taxpayer was chosen under the VAT audit program, the second LOA that covers the regular audit should exclude the VAT. However, any deviation from these rules does not renders the LOA invalid. It only opens the revenue examiners to disciplinary or administrative sanctions. *(Southern Luzon Drug Corporation vs. CIR, CTA Case No. 8941, September 7, 2018).*

Vehicles carrying smuggled goods are exempted from forfeiture if the owner has no knowledge in the transportation of it.

The requirements for exemptions of vehicles, vessels, aircrafts or any other crafts from seizure and forfeiture for carrying or holding on board smuggled goods, are as follows: (1) the vehicles are used as common carriers; (2) not chartered or leased; and (3) the owner or its agents had no knowledge of the unlawful act.

Here, aside from the proven fact that petitioner owns and operates a legitimate business as a common carrier, no evidence was presented before the Court to support the conclusion that the owner has knowledge in the transportation of smuggled goods. *(RS De Vera Trucking vs. COC, CTA Case No. 9521, September 6, 2018).*

The presence of "deliberate" intent is necessary for the conviction of the offense of willful failure to supply correct and accurate information.

The accused was charged for violation of the NIRC for failure to supply correct and accurate information in her annual income tax return and audited financial statements. The accused contends that there is no willful and deliberate intention not to declare and pay taxes on her part.

Here, the Court noted that the prosecution failed to prove intent of accused to deliberately omit the transactions in the ITR and audited financial statements. While the accused may have been negligent in signing documents presented by her husband, without having read the same, said negligence does not equate to willful and deliberate intent.

Hence, failure of the prosecution to present any evidence to prove that the accused willfully failed to file her income tax return, resulting in her failure to pay income taxes due from her for taxable years 2006 to 2009, the Court is duty bound to acquit the accused. (*People vs. Caluag, CTA Crim. Case Nos. O-345, O-346, O-347 and O-348)*.

Dissent of Justice Del Rosario: The accused was registered with the BIR as a One-Time Transaction Taxpayer (ONETT), hence, this circumstance at the very least is indicative of knowledge or awareness on the part of the accused that the transaction generating income or gain is subject to payment of tax with corresponding filing of an appropriate tax return. The filing of an Annual ITR is something that is not unknown or unusual to ordinary taxpayers. *(People vs. Caluag CTA Crim. Case Nos. O-345, O-346, O-347 and O-348).*

Note: **In another case, the Court noted that the taxpayer implicitly admits that she was aware of her duty to file a tax return, and yet failed to do so. This is tantamount to conscious and deliberate failure to file the required return.** *(Caluag vs. People, CTA EB Case No. 047, September 17, 2018).*

A PAN is meaningless to the concept of due process if the taxpayer's right to respond within the prescribed period would be ignored.

Here, the CIR unfairly surprised the taxpayer with Final Assessment Notice (FAN) without waiting for the period within which she could submit it protest to the PAN to expire. More glaring is the obvious fact that the CIR did not even consider the points and arguments of the taxpayer raised in its protest to the PAN prior to issuing a decision on it in the form of the FAN.

The Court emphasized that it is clear from the Tax Code that the right to respond to a PAN is given to the taxpayer, and that the period of fifteen (15) days to file said response is also the

taxpayer's right -- they are not for the CIR to waive. Taxpayer's right to due process has therefore been violated and the FAN is null and void. *(Max's Sta. Mesa, Inc., vs. CIR, CTA Case No. 8786, September 28, 2018).*

Distribution of property dividend is not within the ambit of "other disposition of shares of stock" which recognizes income from disposal.

The taxpayer argues that the provisions of Revenue Regulations (RR) Nos. 6-2008 and 6-2013 apply only to sales, barter, exchange or other disposition, which give rise to the realization of net capital gains subject to capital gains tax. It maintains that its distribution of shares as property dividends was not a sale, barter, exchange or other disposition that would give rise to any realized net capital gains on its part, because it received no consideration for such distribution of dividends. It further alleges that BIR mistakenly treated the property dividend distribution as a transfer for less than an adequate or full consideration or with insufficient consideration, and concluded that there was an indirect gift for the difference between the adjusted fair market value as against the book value of the shares. The Commissioner of Internal Revenue (CIR), on the other hand, insists that donative intent is not necessary for the Tax Code to apply. The taxpayer purportedly became an intentional donor when it distributed shares of stocks as property dividend at a declared value which is lower than that of the fair market value.

The taxpayer argued that it declared and distributed property dividends to its stockholders out of its earnings or profits. The said property dividends distributed were comprised of taxpayer's shares of stock in its wholly-owned subsidiary and were recorded in taxpayer's books at its carrying value. In recording the property dividends at their carrying value, there was no profit or gain realized or recognized in the transaction. Additionally, distribution of property dividends is a non-reciprocal transfer. In other words, there was no consideration given nor received during the transfer.

Here, the Court finds that the corporation's declaration and distribution of property dividend is not within the ambit of the term "other disposition of shares of stock" that would recognize gain or loss from such disposal. Instead, it is a mere equity transaction since taxpayer did not recognize any gain or loss therefrom. *(Trans-Asia and Energy Development Corp., vs. CIR, CTA Case No. 9078, September 28, 2018).*

The waiver is void if not duly notarized.

Here, the Court looks on the validity of the waivers. The Court finds that the first waiver is void as it was not notarized. The Court noted that neither the name of the person who appeared before the notary public nor the detail of his or her identity is indicated. Consequently, since the first waiver is void, it did not extend the 3- year period to assess. There being no more period to extend, the second to the fifth waivers are also void. In conclusion, the Court explained that the doctrine of "in pari delicto" does not apply to this case because there was no intention on the part of the taxpayer to benefit from the infirmity of such waiver. *(Ayala Land Internal Sales, Inc. vs. CIR, CTA Case No. 9262, September 28, 2018).*

The assessment is null and void if not actually received by the taxpayer.

Here, accused Gernale, being the Treasurer of the taxpayer-corporation, was charged of willful failure to pay deficiency income tax and VAT for taxable year 2003. Accused however, avers that she did not receive any notice issued by the BIR. The latter witnesses testified that all notices were served at 1384 Gomez St., Paco, Manila despite the fact that Corporation's principal place of business is in 1331 Burgos St., Paco, Manila.

The Court finds that the evidence of the BIR failed to satisfactorily prove that taxpayer or any of its authorized representatives actually received the PAN. The BIRs witnesses could not positively testify that the PAN was actually received by the Corporation. Hence, the failure of the BIR to prove receipt of the PAN by the taxpayer leads to the conclusion that no assessment was validly issued. Sending of a PAN to taxpayer to inform him of the assessment made is but part of the due process requirement in the issuance of a deficiency tax assessment, the absence of which renders nugatory any assessment made by the tax authorities. *(People vs. Gernale CTA Case No. O-336, September 26, 2018).*

In fact, in one case, the Court held that having established that the taxpayer never received the PAN, the events that came after became irrelevant such as the issuance of the FAN, the filing of the protest, the submission of supporting documents and the issuance of the Final Decision on Disputed Assessment (FDDA). *(CIR vs. Bloat and Ogle, Inc., CTA EB No. 1578, September 18, 2018).*

Note: **In another case however, the Court held that the presumption of regularity in the service of assessment notices by BIR was undisputed. The Court noted that the BIR was able to prove that the letter was properly addressed with postage prepaid and was sent to the registered address of the accused.** *(People vs. Caguimbal CTA Crim. Case Nos. O-546 & O-547, September 26, 2018).*

Royalty income earned in the active pursuit of business is subject to 30% regular corporate tax.

In this case, the taxpayer argues that the income earned from the act of licensing out certain intellectual property rights is merely incidental to taxpayer's primary purpose of business.

During trial, the taxpayer's manager testified that its main line of business is "the manufacturing, buying, selling, and otherwise dealing in alcoholic and non-alcoholic beverages" and that the acquisition of trademarks and other intellectual property rights is merely incidental to it. However, the Court noted that the taxpayer's financial statements shows no operating expenses for its alleged main trade or business of manufacturing, buying, selling and dealing in alcoholic and non-alcoholic beverages. In fact, the financial statements indicate no source of income for both 2009 and 2010 other than taxpayer's royalty income and a minimal amount of interest income.

The Court concludes that the taxpayer's income from licensing put its intellectual property rights is income generated in the active pursuit and performance of its primary purpose, thus, is not passive income. Hence, the royalty income is considered earned in the active pursuit of its trade or business and proper to be subject to the 30% regular income tax. *(Iconic Beverages, Inc. vs. CIR, CTA EB Nos. 1563 & 1564, September 18, 2018).*

Local government units is prohibited from imposing taxes on the National Government, its agencies and instrumentalities.

Here, the Court cited the pronouncement of the Supreme Court (SC) that the SMC shares held by taxpayer are owned by the government. As such, the Court held that since the subject shares are owned by the government, it follows that the dividends and any income derived from it are owned by the government as well, regardless of who has possession of it. That being the case, the subject shares and the dividends from it do not fall within the taxing power of the City of Davao. *(City of Davao vs. Roxas Shares Inc., CTA EB No. 1654, September 17, 2018).*

The sales of a generation company prior to the issuance of the certificate of compliance cannot qualify as zero rated sales.

The instant claim for refund covers input tax incurred for the 3rd quarter of 2008 allegedly attributable to zero-rated sales for the 1st quarter of 2010. However, the Court noted that both these periods come before the issuance of either certificate of compliance (COC) for Plant A or B. Hence, the Court held that although the COCs were eventually issued, the privilege of VAT zero-rating did not retroact to cover the 1st quarter of 2010. *(Hedcor Sibulan, Inc. vs. CIR, CTA EB No. 1641, September 19, 2018).*

Failure to file an application for tax treaty relief does not preclude the taxpayer from enjoying the benefits provided by tax treaty.

Here, CIR argues that any availment of the tax treaty relief should be preceded by an application with International Tax Affairs Division (ITAD) at least 15 days before the transaction accompanies by supporting documents justifying the relief. The Court held that bearing in mind the rationale of tax treaties, the period of application for the availment of tax treaty relief as required by RMO No. 1-2000 should not operate to divest entitlement to the relief as it would constitute a violation of the duty required by good faith in complying with a tax treaty. The denial of the availment of tax relief for the failure of a taxpayer to apply within the prescribed period under the administrative issuance would impair the value of the tax treaty. At most, the application for a tax treaty relief from the BIR should merely operate to confirm the entitlement of the taxpayers to the relief. *(CIR vs. Toyota Motor Philippines, CTA EB No 1688, September 19, 2018).*