496 Phil. 307

THIRD DIVISION

[G.R. NO. 159647, April 15, 2005]

COMMISSIONER OF INTERNAL REVENUE, PETITIONER, VS. CENTRAL LUZON DRUG CORPORATION, RESPONDENT.

D E C I S I O N

PANGANIBAN, J.:

The 20 percent discount required by the law to be given to senior citizens is a *tax credit*, not merely a *tax deduction* from the gross income or gross sale of the establishment concerned. A *tax credit* is used by a private establishment only after the tax has been computed; a *tax deduction*, before the tax is computed. RA 7432 unconditionally grants a *tax credit* to all covered entities. Thus, the provisions of the revenue regulation that withdraw or modify such grant are void. Basic is the rule that administrative regulations cannot amend or revoke the law.

The Case

Before us is a Petition for Review[1] under Rule 45 of the Rules of Court, seeking to set aside the August 29, 2002 Decision[2] and the August 11, 2003 Resolution[3] of the Court of Appeals (CA) in CA-GR SP No. 67439. The assailed Decision reads as follows:

> "**WHEREFORE**, premises considered, the Resolution appealed from is **AFFIRMED** *in toto*. No costs."[4]

The assailed Resolution denied petitioner's Motion for Reconsideration.

The Facts

The CA narrated the antecedent facts as follows:

> "Respondent is a domestic corporation primarily engaged in retailing of medicines and other pharmaceutical products. In 1996, it operated six (6) drugstores under the business name and style 'Mercury Drug.'
>
> "From January to December 1996, respondent granted twenty (20%) percent sales discount to qualified senior citizens on their purchases of medicines pursuant to Republic Act No. [R.A.] 7432 and its Implementing Rules and Regulations. For the said period, the amount allegedly representing the 20% sales discount granted by respondent to qualified senior citizens totaled P904,769.00.
>
> "On April 15, 1997, respondent filed its Annual Income Tax Return for taxable year 1996 declaring therein that it incurred net losses from its operations.

"On January 16, 1998, respondent filed with petitioner a claim for tax refund/credit in the amount of P904,769.00 allegedly arising from the 20% sales discount granted by respondent to qualified senior citizens in compliance with [R.A.] 7432. Unable to obtain affirmative response from petitioner, respondent elevated its claim to the Court of Tax Appeals [(CTA or Tax Court)] via a Petition for Review.

"On February 12, 2001, the Tax Court rendered a Decision[5] dismissing respondent's Petition for lack of merit. In said decision, the [CTA] justified its ruling with the following ratiocination:

> 'x x x, if no tax has been paid to the government, erroneously or illegally, or if no amount is due and collectible from the taxpayer, tax refund or tax credit is unavailing. Moreover, whether the recovery of the tax is made by means of a claim for refund or tax credit, before recovery is allowed[,] it must be first established that there was an actual collection and receipt by the government of the tax sought to be recovered. x x x.
>
> 'x x x x x x x x x
>
> 'Prescinding from the above, it could logically be deduced that tax credit is premised on the existence of tax liability on the part of taxpayer. In other words, if there is no tax liability, tax credit is not available.'

"Respondent lodged a Motion for Reconsideration. The [CTA], in its assailed resolution,[6] granted respondent's motion for reconsideration and ordered herein petitioner to issue a Tax Credit Certificate in favor of respondent citing the decision of the then Special Fourth Division of [the CA] in CA G.R. SP No. 60057 entitled '*Central [Luzon] Drug Corporation vs. Commissioner of Internal Revenue*' promulgated on May 31, 2001, to wit:

> 'However, Sec. 229 clearly does not apply in the instant case because the tax sought to be refunded or credited by petitioner was not erroneously paid or illegally collected. We take exception to the CTA's sweeping but unfounded statement that 'both tax refund and tax credit are modes of recovering taxes which are either erroneously or illegally paid to the government.' Tax refunds or credits do not exclusively pertain to illegally collected or erroneously paid taxes as they may be other circumstances where a refund is warranted. The tax refund provided under Section 229 deals exclusively with illegally collected or erroneously paid taxes but there are other possible situations, such as the refund of excess estimated corporate quarterly income tax paid, or that of excess input tax paid by a VAT-registered person, or that of excise tax paid on goods locally produced or manufactured but actually exported. The standards and mechanics for the grant of a

> refund or credit under these situations are different from that under Sec. 229. Sec. 4[.a)] of R.A. 7432, is yet another instance of a tax credit and it does not in any way refer to illegally collected or erroneously paid taxes, x x x.'"[7]

Ruling of the Court of Appeals

The CA affirmed *in toto* the Resolution of the Court of Tax Appeals (CTA) ordering petitioner to issue a tax credit certificate in favor of respondent in the reduced amount of P903,038.39. It reasoned that Republic Act No. (RA) 7432 required neither a tax liability nor a payment of taxes by private establishments prior to the availment of a tax credit. Moreover, such credit is not tantamount to an unintended benefit from the law, but rather a just compensation for the taking of private property for public use.

Hence this Petition.[8]

The Issues

Petitioner raises the following issues for our consideration:

> "Whether the Court of Appeals erred in holding that respondent may claim the 20% sales discount as a tax credit instead of as a deduction from gross income or gross sales.
>
> "Whether the Court of Appeals erred in holding that respondent is entitled to a refund."[9]

These two issues may be summed up in only one: whether respondent, despite incurring a net loss, may still claim the 20 percent sales discount as a tax credit.

The Court's Ruling

The Petition is not meritorious.

Sole Issue:
Claim of 20 Percent Sales Discount as Tax Credit Despite Net Loss

Section 4a) of RA 7432[10] grants to senior citizens the privilege of obtaining a 20 percent discount on their purchase of medicine from any private establishment in the country.[11] The latter may then claim the cost of the discount as a *tax credit*.[12] But can such credit be claimed, even though an establishment operates at a loss?

We answer in the affirmative.

Tax Credit *versus* Tax Deduction

Although the term is not specifically defined in our Tax Code,[13] *tax credit* generally

refers to an amount that is "subtracted directly from one's total tax liability."[14] It is an "allowance against the tax itself"[15] or "a deduction from what is owed"[16] by a taxpayer to the government. Examples of *tax credits* are withheld taxes, payments of estimated tax, and investment tax credits.[17]

Tax credit should be understood in relation to other tax concepts. One of these is *tax deduction* -- defined as a subtraction "from income for tax purposes,"[18] or an amount that is "allowed by law to reduce income prior to [the] application of the tax rate to compute the amount of tax which is due."[19] An example of a *tax deduction* is any of the allowable deductions enumerated in Section 34[20] of the Tax Code.

A *tax credit* differs from a *tax deduction*. On the one hand, a *tax credit* reduces the tax due, including -- whenever applicable -- the *income tax* that is determined after applying the corresponding tax rates to *taxable income*.[21] A *tax deduction*, on the other, reduces the income that is subject to tax[22] in order to arrive at *taxable income*.[23] To think of the former as the latter is to avoid, if not entirely confuse, the issue. A *tax credit* is used only after the tax has been computed; a *tax deduction*, **before**.

Tax Liability Required for Tax Credit

Since a *tax credit* is used to reduce directly the tax that is due, there ought to be a tax liability **before** the *tax credit* can be applied. Without that liability, any *tax credit* application will be useless. There will be no reason for deducting the latter when there is, to begin with, no existing obligation to the government. However, as will be presented shortly, the *existence* of a tax credit or its *grant* by law is not the same as the *availment* or *use* of such credit. While the grant is mandatory, the availment or use is not.

If a *net loss* is reported by, and no other taxes are currently due from, a business establishment, there will obviously be no tax liability against which any *tax credit* can be applied.[24] For the establishment to choose the immediate availment of a *tax credit* will be premature and impracticable. Nevertheless, the irrefutable fact remains that, under RA 7432, Congress has granted without conditions a tax credit benefit to all covered establishments.

Although this *tax credit* benefit is available, it need not be used by losing ventures, since there is no tax liability that calls for its application. Neither can it be reduced to nil by the quick yet callow stroke of an administrative pen, simply because no reduction of taxes can instantly be effected. By its nature, the *tax credit* may still be deducted from a *future*, not a *present*, tax liability, without which it does not have any use. In the meantime, it need not move. But it breathes.

Prior Tax Payments Not Required for Tax Credit

While a tax liability is essential to the *availment or use* of any *tax credit*, prior tax payments are not. On the contrary, for the *existence or grant* solely of such credit, neither a tax liability nor a prior tax payment is needed. The Tax Code is in fact

replete with provisions granting or allowing *tax credits*, even though no taxes have been previously paid.

For example, in computing the *estate tax due*, Section 86(E) allows a *tax credit* -- subject to certain limitations -- for estate taxes paid to a foreign country. Also found in Section 101(C) is a similar provision for donor's taxes -- again when paid to a foreign country -- in computing for the *donor's tax due*. The *tax credits* in both instances allude to the prior payment of taxes, even if not made to our government.

Under Section 110, a VAT (Value-Added Tax)- registered person engaging in transactions -- whether or not subject to the VAT -- is also allowed a *tax credit* that includes a ratable portion of any input tax not directly attributable to either activity. This input tax may *either* be the VAT on the purchase or importation of goods or services that is merely due from -- not necessarily paid by -- such VAT-registered person in the course of trade or business; *or* the transitional input tax determined in accordance with Section 111(A). The latter type may in fact be an amount equivalent to only eight percent of the value of a VAT-registered person's beginning inventory of goods, materials and supplies, when such amount -- as computed -- is higher than the actual VAT paid on the said items.[25] Clearly from this provision, the *tax credit* refers to an input tax that is either due only or given a value by mere comparison with the VAT actually paid -- then later prorated. No tax is actually paid prior to the availment of such credit.

In Section 111(B), a one and a half percent input *tax credit* that is merely presumptive is allowed. For the purchase of primary agricultural products used as inputs --either in the processing of sardines, mackerel and milk, or in the manufacture of refined sugar and cooking oil -- and for the contract price of public work contracts entered into with the government, again, no prior tax payments are needed for the use of the *tax credit*.

More important, a VAT-registered person whose sales are zero-rated or effectively zero-rated may, under Section 112(A), apply for the issuance of a *tax credit* certificate for the amount of creditable input taxes merely due -- again not necessarily paid to -- the government and attributable to such sales, to the extent that the input taxes have not been applied against output taxes.[26] Where a taxpayer is engaged in zero-rated or effectively zero-rated sales and also in taxable or exempt sales, the amount of creditable input taxes due that are not directly and entirely attributable to any one of these transactions shall be proportionately allocated on the basis of the volume of sales. Indeed, in availing of such *tax credit* for VAT purposes, this provision -- as well as the one earlier mentioned -- shows that the prior payment of taxes is not a requisite.

It may be argued that Section 28(B)(5)(b) of the Tax Code is another illustration of a *tax credit* allowed, even though no prior tax payments are not required. Specifically, in this provision, the imposition of a final withholding tax rate on cash and/or property dividends received by a nonresident foreign corporation from a domestic corporation is subjected to the condition that a foreign *tax credit* will be given by the domiciliary country in an amount equivalent to taxes that are merely deemed paid.[27] Although true, this provision actually refers to the *tax credit* as a *condition* only for the imposition of a lower tax rate, not as a *deduction* from the corresponding tax liability. Besides, it is not our government but the domiciliary