

## FIRST DIVISION

[ G.R. No. 159610, June 12, 2008 ]

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

#### D E C I S I O N

**CARPIO, J.:**

##### The Case

This petition for review on certiorari<sup>[1]</sup> assails the 13 August 2003 Decision<sup>[2]</sup> of the Court of Appeals in CA-G.R. SP No. 70480. The Court of Appeals dismissed the appeal filed by the Commissioner of Internal Revenue (petitioner) questioning the 15 April 2002 Decision<sup>[3]</sup> of the Court of Tax Appeals (CTA) in CTA Case No. 6054 ordering petitioner to issue, in favor of Central Luzon Drug Corporation (respondent), a tax credit certificate in the amount of P2,376,805.63, arising from the alleged erroneous interpretation of the term "tax credit" used in Section 4(a) of Republic Act No. (RA) 7432.<sup>[4]</sup>

##### The Facts

Respondent is a domestic corporation engaged in the retail of medicines and other pharmaceutical products.<sup>[5]</sup> In 1997, it operated eight drugstores under the business name and style "Mercury Drug."<sup>[6]</sup>

Pursuant to the provisions of RA 7432 and Revenue Regulations No. (RR) 2-94<sup>[7]</sup> issued by the Bureau of Internal Revenue (BIR), respondent granted 20% sales discount to qualified senior citizens on their purchases of medicines covering the calendar year 1997. The sales discount granted to senior citizens totaled P2,798,508.00.

On 15 April 1998, respondent filed its 1997 Corporate Annual Income Tax Return reflecting a nil income tax liability due to net loss incurred from business operations of P2,405,140.00.<sup>[8]</sup> Respondent filed its 1997 Income Tax Return under protest.<sup>[9]</sup>

On 19 March 1999, respondent filed with the petitioner a claim for refund or credit of overpaid income tax for the taxable year 1997 in the amount of P2,660,829.00.<sup>[10]</sup> Respondent alleged that the overpaid tax was the result of the wrongful implementation of RA 7432. Respondent treated the 20% sales discount as a deduction from gross sales in compliance with RR 2-94 instead of treating it as a tax credit as provided under Section 4(a) of RA 7432.

On 6 April 2000, respondent filed a Petition for Review with the CTA in order to toll the running of the two-year statutory period within which to file a judicial claim.

Respondent reasoned that RR 2-94, which is a mere implementing administrative regulation, cannot modify, alter or amend the clear mandate of RA 7432. Consequently, Section 2(i) of RR 2-94 is without force and effect for being inconsistent with the law it seeks to implement.<sup>[11]</sup>

In his Answer, petitioner stated that the construction given to a statute by a specialized administrative agency like the BIR is entitled to great respect and should be accorded great weight. When RA 7432 allowed senior citizens' discounts to be claimed as tax credit, it was silent as to the mechanics of availing the same. For clarification, the BIR issued RR 2-94 and defined the term "tax credit" as a deduction from the establishment's gross income and not from its tax liability in order to avoid an absurdity that is not intended by the law. <sup>[12]</sup>

### **The Ruling of the Court of Tax Appeals**

On 15 April 2002, the CTA rendered a Decision ordering petitioner to issue a tax credit certificate in the amount of P2,376,805.63 in favor of respondent.

The CTA stated that in a number of analogous cases, it has consistently ruled that the 20% senior citizens' discount should be treated as tax credit instead of a mere deduction from gross income.<sup>[13]</sup> In quoting its previous decisions, the CTA ruled that RR 2-94 engraved a new meaning to the phrase "tax credit" as deductible from gross income which is a deviation from the plain intendment of the law. An administrative regulation must not contravene but should conform to the standards that the law prescribes.<sup>[14]</sup>

The CTA also ruled that respondent has properly substantiated its claim for tax credit by documentary evidence. However, based on the examination conducted by the commissioned independent certified public accountant (CPA), there were some material discrepancies due to missing cash slips, lack of senior citizen's ID number, failure to include the cash slips in the summary report and vice versa. Therefore, between the Summary Report presented by respondent and the audited amount presented by the independent CPA, the CTA deemed it proper to consider the lesser of two amounts.

The re-computation of the overpaid income tax<sup>[15]</sup> for the year 1997 is as follows:

Sales, Net		P 176,742,607.00
Add: 20% Sales Discount to Senior Citizens		<u>2,798,508.00</u>
Sales, Gross		P 179,541,115.00
Less: Cost of Sales		
Merchandise inventory, beg.	P 20,905,489.00	
Purchases	168,762,950.00	
Merchandise inventory, end	<u>—(27,281,439.00)</u>	<u>162,387,000.00</u>
Gross Profit		P 17,154,115.00
Add: Miscellaneous income		<u>402,124.00</u>
Total Income		P 17,556,239.00
Less: Operating expenses		<u>16,913,699.00</u>
Net Income		P 642,540.00

Less: Income subjected to final tax (Interest Income <sup>[16]</sup> )	249,172.00
Net Taxable Income	P 393,368.00
Income Tax Due (35%)	P 137,679.00
Less: Tax Credit (Cost of 20% discount as adjusted <sup>[17]</sup> )	2,514,484.63
Income Tax Payable	(P 2,376,805.63)
Income Tax Actually Paid	0.00
Income Tax Refundable	(P 2,376,805.63)

Aggrieved by the CTA's decision, petitioner elevated the case before the Court of Appeals.

### **The Ruling of the Appellate Court**

On 13 August 2003, the Court of Appeals affirmed the CTA's decision *in toto*.

The Court of Appeals disagreed with petitioner's contention that the CTA's decision applied a literal interpretation of the law. It reasoned that under the *verba legis* rule, if the statute is clear, plain, and free from ambiguity, it must be given its literal meaning and applied without interpretation. This principle rests on the presumption that the words used by the legislature in a statute correctly express its intent and preclude the court from construing it differently.<sup>[18]</sup>

The Court of Appeals distinguished "tax credit" as an amount subtracted from a taxpayer's total tax liability to arrive at the tax due while a "tax deduction" reduces the taxpayer's taxable income upon which the tax liability is computed. "A credit differs from deduction in that the former is subtracted from tax while the latter is subtracted from income before the tax is computed."<sup>[19]</sup>

The Court of Appeals found no legal basis to support petitioner's opinion that actual payment by the taxpayer or actual receipt by the government of the tax sought to be credited or refunded is a condition *sine qua non* for the availment of tax credit as enunciated in Section 229<sup>[20]</sup> of the Tax Code. The Court of Appeals stressed that Section 229 of the Tax Code pertains to illegally collected or erroneously paid taxes while RA 7432 is a special law which uses the method of tax credit in the context of just compensation. Further, RA 7432 does not require prior tax payment as a condition for claiming the cost of the sales discount as tax credit.

Hence, this petition.

### **The Issues**

Petitioner raises two issues<sup>[21]</sup> in this Petition:

1. Whether the appellate court erred in holding that respondent may claim the 20% senior citizens' sales discount as a tax credit deductible from future income tax liabilities instead of a mere deduction from gross income or gross sales; and

2. Whether the appellate court erred in holding that respondent is entitled to a refund.

### **The Ruling of the Court**

The petition lacks merit.

The issues presented are not novel. In two similar cases involving the same parties where respondent lodged its claim for tax credit on the senior citizens' discount granted in 1995<sup>[22]</sup> and 1996,<sup>[23]</sup> this Court has squarely ruled that the 20% senior citizens' discount required by RA 7432 may be claimed as a tax credit and not merely a tax deduction from gross sales or gross income. Under RA 7432, Congress granted the tax credit benefit to all covered establishments without conditions. The net loss incurred in a taxable year does not preclude the grant of tax credit because by its nature, the tax credit may still be deducted from a future, not a present, tax liability. However, the senior citizens' discount granted as a tax credit cannot be refunded.

***RA 7432 expressly allows private establishments  
to claim the amount of discounts they grant to senior citizens  
as tax credit.***

Section 4(a) of RA 7432 states:

SECTION 4. *Privileges for the Senior Citizens.* - The senior citizens shall be entitled to the following:

a) **the grant of twenty percent (20%) discount from** all establishments relative to the utilization of transportation services, hotels and similar lodging establishments, restaurants and recreation centers and **purchase of medicines** anywhere in the country: Provided, That **private establishments may claim the cost as tax credit;** (Emphasis supplied)

However, RR 2-94 interpreted the tax credit provision of RA 7432 in this wise:

Sec. 2. DEFINITIONS. - For purposes of these regulations:

x x x

i. Tax Credit - refers to the **amount representing 20% discount granted to a qualified senior citizen** by all establishments relative to their utilization of transportation services, hotels and similar lodging establishments, restaurants, drugstores, recreation centers, theaters, cinema houses, concert halls, circuses, carnivals and other similar places of culture, leisure and amusement, which **discount shall be deducted by the said establishments from their gross income for income tax purposes** and from their gross sales for value-added tax or other percentage tax purposes. (Emphasis supplied).

x x x

Sec. 4. Recording/Bookkeeping Requirement for Private Establishments