Republic of the Philippines
Supreme Court
Manila

SECOND DIVISION

SMI-ED PHILIPPINES TECHNOLOGY, INC., Petitioner,	**G.R. No. 175410** Present:
-versus-	CARPIO, *J., Chairperson,* BRION, DEL CASTILLO, MENDOZA, and LEONEN, *JJ.*
COMMISSIONER OF INTERNAL REVENUE, Respondent.	**Promulgated:** NOV 12 2014

x----------x

DECISION

LEONEN, *J.*:

In an action for the refund of taxes allegedly erroneously paid, the Court of Tax Appeals may determine whether there are taxes that should have been paid in lieu of the taxes paid. Determining the proper category of tax that should have been paid is not an assessment. It is incidental to determining whether there should be a refund.

A Philippine Economic Zone Authority (PEZA)-registered corporation that has never commenced operations may not avail the tax incentives and preferential rates given to PEZA-registered enterprises. Such corporation is subject to ordinary tax rates under the National Internal Revenue Code of 1997.

This is a petition for review[1] on certiorari of the November 3, 2006 Court of Tax Appeals En Banc decision.[2] It affirmed the Court of Tax Appeals Second Division's decision[3] and resolution[4] denying petitioner SMI-Ed Philippines Technology, Inc.'s (SMI-Ed Philippines) claim for tax refund.[5]

SMI-Ed Philippines is a PEZA-registered corporation authorized "to engage in the business of manufacturing ultra high-density microprocessor unit package."[6]

After its registration on June 29, 1998, SMI-Ed Philippines constructed buildings and purchased machineries and equipment.[7] As of December 31, 1999, the total cost of the properties amounted to □3,150,925,917.00.[8]

SMI-Ed Philippines "failed to commence operations."[9] Its factory was temporarily closed, effective October 15, 1999. On August 1, 2000, it sold its buildings and some of its installed machineries and equipment to Ibiden Philippines, Inc., another PEZA-registered enterprise, for ¥2,100,000,000.00 (□893,550,000.00). SMI-Ed Philippines was dissolved on November 30, 2000.[10]

In its quarterly income tax return for year 2000, SMI-Ed Philippines subjected the entire gross sales of its properties to 5% final tax on PEZA-registered corporations. SMI-Ed Philippines paid taxes amounting to □44,677,500.00.[11]

On February 2, 2001, after requesting the cancellation of its PEZA registration and amending its articles of incorporation to shorten its corporate term, SMI-Ed Philippines filed an administrative claim for the refund of □44,677,500.00 with the Bureau of Internal Revenue (BIR). SMI-Ed Philippines alleged that the amount was erroneously paid. It also indicated the refundable amount in its final income tax return filed on March

---

1 *Rollo*, pp. 29–51.
2 Id. at 7–19. The decision was penned by Associate Justice Lovell R. Bautista and concurred in by Associate Justices Juanito C. Castañeda, Jr., Erlinda P. Uy, Caesar A. Casanova and Olga Palanca-Enriquez. Presiding Justice Ernesto D. Acosta penned a concurring and dissenting opinion.
3 Id. at 54–68. The decision was penned by Associate Justice Juanito C. Castañeda, Jr. (Chair) and concurred in by Associate Justices Erlinda P. Uy and Olga Palanca-Enriquez.
4 Id. at 93–101. The resolution was penned by Associate Justice Juanito C. Castañeda, Jr. (Chair) and concurred in by Associate Justices Erlinda P. Uy and Olga Palanca-Enriquez.
5 Id. at 18.
6 Id. at 8.
7 Id.
8 Id. at 8 and 35.
9 Id. at 8.
10 Id. at 8–9 and 35.
11 Id. at 9 and 35.

1, 2001. It also alleged that it incurred a net loss of □2,233,464,538.00.[12]

The BIR did not act on SMI-Ed Philippines' claim, which prompted the latter to file a petition for review before the Court of Tax Appeals on September 9, 2002.[13]

The Court of Tax Appeals Second Division denied SMI-Ed Philippines' claim for refund in the decision dated December 29, 2004.[14]

The Court of Tax Appeals Second Division found that SMI-Ed Philippines' administrative claim for refund and the petition for review with the Court of Tax Appeals were filed within the two-year prescriptive period.[15] However, fiscal incentives given to PEZA-registered enterprises may be availed only by PEZA-registered enterprises that had already commenced operations.[16] Since SMI-Ed Philippines had not commenced operations, it was not entitled to the incentives of either the income tax holiday or the 5% preferential tax rate.[17] Payment of the 5% preferential tax amounting to □44,677,500.00 was erroneous.[18]

After finding that SMI-Ed Philippines sold properties that were capital assets under Section 39(A)(1) of the National Internal Revenue Code of 1997, the Court of Tax Appeals Second Division subjected the sale of SMI-Ed Philippines' assets to 6% capital gains tax under Section 27(D)(5) of the same Code and Section 2 of Revenue Regulations No. 8-98.[19] It was found liable for capital gains tax amounting to □53,613,000.00.[20] Therefore, SMI-Ed Philippines must still pay the balance of □8,935,500.00 as deficiency tax,[21] "which respondent should perhaps look into."[22] The dispositive portion of the Court of Tax Appeals Second Division's decision reads:

> **WHEREFORE,** premises considered, the instant petition is hereby **DENIED.**
>
> **SO ORDERED.**[23]

The Court of Tax Appeals denied SMI-Ed Philippines' motion for

---

12 Id. at 9 and 35–36.
13 Id. at 9.
14 Id. at 10.
15 Id. at 60.
16 Id. at 61–62.
17 Id. at 62.
18 Id.
19 Id. at 63–67.
20 Id. at 68.
21 Id. "[H]aving paid already . . . the amount of P44,677,500.00"
22 Id.
23 Id.

reconsideration in its June 15, 2005 resolution.[24]

On July 17, 2005, SMI-Ed Philippines filed a petition for review before the Court of Tax Appeals En Banc.[25] It argued that the Court of Tax Appeals Second Division erroneously assessed the 6% capital gains tax on the sale of SMI-Ed Philippines' equipment, machineries, and buildings.[26] It also argued that the Court of Tax Appeals Second Division cannot make an assessment at the first instance.[27] Even if the Court of Tax Appeals Second Division has such power, the period to make an assessment had already prescribed.[28]

In the decision promulgated on November 3, 2006, the Court of Tax Appeals En Banc dismissed SMI-Ed Philippines' petition and affirmed the Court of Tax Appeals Second Division's decision and resolution.[29] The dispositive portion of the Court of Tax Appeals En Banc's decision reads:

> **WHEREFORE,** finding no reversible error to reverse the assailed Decision promulgated on December 29, 2004 and the Resolution dated June 15, 2005, the instant petition for review is hereby DISMISSED. Accordingly, the assailed Decision and Resolution are hereby **AFFIRMED.**
>
> **SO ORDERED.**[30]

SMI-Ed Philippines filed a petition for review before this court on December 27, 2006,[31] praying for the grant of its claim for refund and the reversal of the Court of Tax Appeals En Banc's decision.[32]

SMI-Ed Philippines assigned the following errors:

> A. The honorable CTA *En Banc* grievously erred and acted beyond its jurisdiction when it assessed for deficiency tax in the first instance.
>
> B. Even assuming that the honorable CTA *En Banc* has the right to make an assessment against the petitioner-appellant, it grievously erred in finding that the machineries and equipment sold by the petitioner-appellant is subject to the six percent (6%) capital gains tax under Section 27(D)(5) of the Tax Code.[33]

---

24 Id.at 10.
25 Id. at 36.
26 Id. at 10–11 and 114.
27 Id. at 11 and 114.
28 Id.
29 Id. at 18.
30 Id.
31 Id. at 29.
32 Id. at 50.
33 Id. at 37.

Petitioner argued that the Court of Tax Appeals has no jurisdiction to make an assessment since its jurisdiction, with respect to the decisions of respondent, is merely appellate.[34] Moreover, the power to make assessment had already prescribed under Section 203 of the National Internal Revenue Code of 1997 since the return for the erroneous payment was filed on September 13, 2000. This is more than three (3) years from the last day prescribed by law for the filing of the return.[35]

Petitioner also argued that the Court of Tax Appeals En Banc erroneously subjected petitioner's machineries to 6% capital gains tax.[36] Section 27(D)(5) of the National Internal Revenue Code of 1997 is clear that the 6% capital gains tax on domestic corporations applies only on the sale of lands and buildings and not to machineries and equipment.[37] Since ¥1,700,000,000.00 of the ¥2,100,000,000.00 constituted the consideration for the sale of petitioner's machineries, only ¥400,000,000.00 or □170,200,000.00 should be subjected to the 6% capital gains tax.[38] Petitioner should be liable only for □10,212,000.00.[39] It should be entitled to a refund of □34,464,500.00 after deducting □10,212,000.00 from the erroneously paid final tax of □44,677,500.00.[40]

In its comment, respondent argued that the Court of Tax Appeals' determination of petitioner's liability for capital gains tax was not an assessment. Such determination was necessary to settle the question regarding the tax consequence of the sale of the properties.[41] This is clearly within the Court of Tax Appeals' jurisdiction under Section 7 of Republic Act No. 9282.[42] Respondent also argued that "petitioner failed to justify its claim for refund."[43]

The petition is meritorious.

I
Jurisdiction of the Court of Tax Appeals

The term "assessment" refers to the determination of amounts due from a person obligated to make payments. In the context of national internal revenue collection, it refers the determination of the taxes due from a taxpayer under the National Internal Revenue Code of 1997.

---

34 Id. at 38.
35 Id. at 40–41.
36 Id. at 41.
37 Id. at 30–31.
38 Id. at 46–47.
39 Id. at 47.
40 Id.
41 Id. at 210.
42 Id. at 210–212.
43 Id. at 218.

The power and duty to assess national internal revenue taxes are lodged with the BIR.[44] Section 2 of the National Internal Revenue Code of 1997 provides:

> SEC. 2. Powers and Duties of the Bureau of Internal Revenue. - The Bureau of Internal Revenue shall be under the supervision and control of the Department of Finance and *its powers and duties shall comprehend the assessment and collection of all national internal revenue taxes, fees, and charges*, and the enforcement of all forfeitures, penalties, and fines connected therewith, including the execution of judgments in all cases decided in its favor by the Court of Tax Appeals and the ordinary courts. The Bureau shall give effect to and administer the supervisory and police powers conferred to it by this Code or other laws. (Emphasis supplied)

The BIR is not mandated to make an assessment relative to every return filed with it. Tax returns filed with the BIR enjoy the presumption that these are in accordance with the law.[45] Tax returns are also presumed correct since these are filed under the penalty of perjury.[46] Generally, however, the BIR assesses taxes when it appears, after a return had been filed, that the taxes paid were incorrect,[47] false,[48] or fraudulent.[49] The BIR also assesses taxes when taxes are due but no return is filed.[50] Thus:

> **SEC. 6. Power of the Commissioner to Make assessments and Prescribe additional Requirements for Tax Administration and Enforcement.–**
>
> (A) Examination of Returns and Determination of Tax Due. - *After a return has been filed* as required under the provisions of this Code, the Commissioner or his duly authorized representative may authorize the examination of any taxpayer and *the assessment of the correct amount of tax*: Provided, however; *That failure to file a return shall not prevent the Commissioner from authorizing the examination of any taxpayer.* The tax or any deficiency tax so assessed shall be paid upon notice and demand from the Commissioner or from his duly authorized representative.
>
> . . . .
>
> **SEC. 222. Exceptions as to Period of Limitation of Assessment and Collection of Taxes.**
>
> (a) In the case of a *false or fraudulent return with intent to evade tax or of failure to file a return*, the tax may be assessed, or a preceeding in court for the collection of such tax may be filed

---

44 TAX CODE, sec. 2.
45 RULES OF COURT, Rule 131, sec. 3(ff).
46 TAX CODE, sec. 267.
47 TAX CODE, sec. 6.
48 TAX CODE, sec. 222.
49 TAX CODE, sec. 222.
50 TAX CODE, sec. 6 and 222.

> without assessment, at any time within ten (10) years after the discovery of the falsity, fraud or omission: Provided, That in a fraud assessment which has become final and executory, the fact of fraud shall be judicially taken cognizance of in the civil or criminal action for the collection thereof. (Emphasis supplied)

The Court of Tax Appeals has no power to make an assessment at the first instance. On matters such as tax collection, tax refund, and others related to the national internal revenue taxes, the Court of Tax Appeals' jurisdiction is appellate in nature.

Section 7(a)(1) and Section 7(a)(2) of Republic Act No. 1125,[51] as amended by Republic Act No. 9282,[52] provide that the Court of Tax Appeals reviews decisions and inactions of the Commissioner of Internal Revenue in disputed assessments and claims for tax refunds. Thus:

> SEC. 7. *Jurisdiction.* - The CTA shall exercise:
>
> a. Exclusive appellate jurisdiction to review by appeal, as herein provided:
>
> 1. *Decisions of the Commissioner of Internal Revenue in cases involving disputed assessments, refunds of internal revenue taxes*, fees or other charges, penalties in relation thereto, or other matters arising under the National Internal Revenue or other laws administered by the Bureau of Internal Revenue;
>
> 2. *Inaction by the Commissioner of Internal Revenue in cases involving disputed assessments, refunds of internal revenue taxes*, fees or other charges, penalties in relations thereto, or other matters arising under the National Internal Revenue Code or other laws administered by the Bureau of Internal Revenue, where the National Internal Revenue Code provides a specific period of action, in which case the inaction shall be deemed a denial[.] (Emphasis supplied)

Based on these provisions, the following must be present for the Court of Tax Appeals to have jurisdiction over a case involving the BIR's decisions or inactions:

a) A case involving any of the following:

   i. Disputed assessments;
   ii. Refunds of internal revenue taxes, fees, or other charges,

---

51 An Act Creating the Court of Tax Appeals (1954).

52 An Act Expanding the Jurisdiction of the Court of Tax Appeals (CTA), Elevating its Rank to the Level of a Collegiate Court with Special Jurisdiction and Enlarging its Membership, Amending for the Purpose Certain Sections or Republic Act No. 1125, as amended, Otherwise Known as the Law Creating the Court of Tax Appeals, and for Other Purposes (2004).

penalties in relation thereto; and

iii. Other matters arising under the National Internal Revenue Code of 1997.

b) Commissioner of Internal Revenue's decision or inaction in a case submitted to him or her

Thus, the BIR first has to make an assessment of the taxpayer's liabilities. When the BIR makes the assessment, the taxpayer is allowed to dispute that assessment before the BIR. If the BIR issues a decision that is unfavorable to the taxpayer or if the BIR fails to act on a dispute brought by the taxpayer, the BIR's decision or inaction may be brought on appeal to the Court of Tax Appeals. The Court of Tax Appeals then acquires jurisdiction over the case.

When the BIR's unfavorable decision is brought on appeal to the Court of Tax Appeals, the Court of Tax Appeals reviews the correctness of the BIR's assessment and decision. In reviewing the BIR's assessment and decision, the Court of Tax Appeals had to make its own determination of the taxpayer's tax liabilities. The Court of Tax Appeals may not make such determination before the BIR makes its assessment and before a dispute involving such assessment is brought to the Court of Tax Appeals on appeal.

The Court of Tax Appeals' jurisdiction is not limited to cases when the BIR makes an assessment or a decision unfavorable to the taxpayer. Because Republic Act No. 1125[53] also vests the Court of Tax Appeals with jurisdiction over the BIR's inaction on a taxpayer's refund claim, there may be instances when the Court of Tax Appeals has to take cognizance of cases that have nothing to do with the BIR's assessments or decisions. When the BIR fails to act on a claim for refund of voluntarily but mistakenly paid taxes, for example, there is no decision or assessment involved.

Taxes are generally self-assessed. They are initially computed and voluntarily paid by the taxpayer. The government does not have to demand it. If the tax payments are correct, the BIR need not make an assessment.

The self-assessing and voluntarily paying taxpayer, however, may later find that he or she has erroneously paid taxes. Erroneously paid taxes may come in the form of amounts that should not have been paid. Thus, a taxpayer may find that he or she has paid more than the amount that should have been paid under the law. Erroneously paid taxes may also come in the form of tax payments for the wrong category of tax. Thus, a taxpayer may find that he or she has paid a certain kind of tax that he or she is not subject to.

---

[53] As amended by Republic Act No. 9282.

In these instances, the taxpayer may ask for a refund. If the BIR fails to act on the request for refund, the taxpayer may bring the matter to the Court of Tax Appeals.

From the taxpayer's self-assessment and tax payment up to his or her request for refund and the BIR's inaction, the BIR's participation is limited to the receipt of the taxpayer's payment. The BIR does not make an assessment; the BIR issues no decision; and there is no dispute yet involved.

Since there is no BIR assessment yet, the Court of Tax Appeals may not determine the amount of taxes due from the taxpayer. There is also no decision yet to review. However, there was inaction on the part of the BIR. That inaction is within the Court of Tax Appeals' jurisdiction.

In other words, the Court of Tax Appeals may acquire jurisdiction over cases even if they do not involve BIR assessments or decisions.

In this case, the Court of Tax Appeals' jurisdiction was acquired because petitioner brought the case on appeal before the Court of Tax Appeals after the BIR had failed to act on petitioner's claim for refund of erroneously paid taxes. The Court of Tax Appeals did not acquire jurisdiction as a result of a disputed assessment of a BIR decision.

Petitioner argued that the Court of Tax Appeals had no jurisdiction to subject it to 6% capital gains tax or other taxes at the first instance. The Court of Tax Appeals has no power to make an assessment.

As earlier established, the Court of Tax Appeals has no assessment powers. In stating that petitioner's transactions are subject to capital gains tax, however, the Court of Tax Appeals was not making an assessment. It was merely determining the proper category of tax that petitioner should have paid, in view of its claim that it erroneously imposed upon itself and paid the 5% final tax imposed upon PEZA-registered enterprises.

The determination of the proper category of tax that petitioner should have paid is an incidental matter necessary for the resolution of the principal issue, which is whether petitioner was entitled to a refund. [54]

The issue of petitioner's claim for tax refund is intertwined with the issue of the proper taxes that are due from petitioner. A claim for tax refund

---

[54] *See Collector of Internal Revenue v. Lacson*, 107 Phil. 945, 947–948 (1960) [Per C.J. Paras, En Banc].

carries the assumption that the tax returns filed were correct.[55] If the tax return filed was not proper, the correctness of the amount paid and, therefore, the claim for refund become questionable. In that case, the court must determine if a taxpayer claiming refund of erroneously paid taxes is more properly liable for taxes other than that paid.

In *South African Airways v. Commissioner of Internal Revenue,*[56] South African Airways claimed for refund of its erroneously paid 2½% taxes on its gross Philippine billings. This court did not immediately grant South African's claim for refund. This is because although this court found that South African Airways was not subject to the 2½% tax on its gross Philippine billings, this court also found that it was subject to 32% tax on its taxable income.[57]

In this case, petitioner's claim that it erroneously paid the 5% final tax is an admission that the quarterly tax return it filed in 2000 was improper. Hence, to determine if petitioner was entitled to the refund being claimed, the Court of Tax Appeals has the duty to determine if petitioner was indeed not liable for the 5% final tax and, instead, liable for taxes other than the 5% final tax. As in *South African Airways,* petitioner's request for refund can neither be granted nor denied outright without such determination.[58]

If the taxpayer is found liable for taxes other than the erroneously paid 5% final tax, the amount of the taxpayer's liability should be computed and deducted from the refundable amount.

Any liability in excess of the refundable amount, however, may not be collected in a case involving solely the issue of the taxpayer's entitlement to refund. The question of tax deficiency is distinct and unrelated to the question of petitioner's entitlement to refund. Tax deficiencies should be subject to assessment procedures and the rules of prescription. The court cannot be expected to perform the BIR's duties whenever it fails to do so either through neglect or oversight. Neither can court processes be used as a tool to circumvent laws protecting the rights of taxpayers.

II
Petitioner's entitlement to benefits given to PEZA-registered enterprises

Petitioner is not entitled to benefits given to PEZA-registered enterprises, including the 5% preferential tax rate under Republic Act No.

---

55 *South African Airways v. Commissioner of Internal Revenue*, G.R. No. 180356, February 16, 2010, 612 SCRA 665, 682 [Per J. Velasco, Jr., Third Division].

56 G.R. No. 180356, February 16, 2010, 612 SCRA 665 [Per J. Velasco, Jr., Third Division].

57 Id. at 682–683.

58 Id. at 683.

7916 or the Special Economic Zone Act of 1995. This is because it never began its operation.

Essentially, the purpose of Republic Act No. 7916 is to promote development and encourage investments and business activities that will generate employment.[59] Giving fiscal incentives to businesses is one of the means devised to achieve this purpose. It comes with the expectation that persons who will avail these incentives will contribute to the purpose's achievement. Hence, to avail the fiscal incentives under Republic Act No. 7916, the law did not say that mere PEZA registration is sufficient.

Republic Act No. 7916 or The Special Economic Zone Act of 1995 provides:

> SEC. 23. *Fiscal Incentives.* — Business establishments *operating within the ECOZONES* shall be entitled to the fiscal incentives as provided for under Presidential Decree No. 66, the law creating the Export Processing Zone Authority, or those provided under Book VI of Executive Order No. 226, otherwise known as the Omnibus Investment Code of 1987.
>
> Furthermore, tax credits for exporters using local materials as inputs shall enjoy the same benefits provided for in the Export Development Act of 1994.
>
> SEC. 24. *Exemption from Taxes Under the National Internal Revenue Code*. — Any provision of existing laws, rules and regulations to the contrary notwithstanding, no taxes, local and national, shall be imposed on *business establishments operating within the ECOZONE.* In lieu of paying taxes, five percent (5%) of the gross income earned by all businesses and enterprises within the ECOZONE shall be remitted to the national government. This five percent (5%) shall be shared and distributed as follows:
>
> a. Three percent (3%) to the national government;
> b. One percent (1%) to the local government units affected by the declaration of the ECOZONE in proportion to their population, land area, and equal sharing factors; and
> c. One percent (1%) for the establishment of a development fund to be utilized for the development of municipalities outside and contiguous to each ECOZONE: *Provided, however*, That the respective share of the affected local government units shall be determined on the basis of the following formula:
>
> 1. Population - fifty percent (50%);
> 2. Land area - twenty-five percent (25%); and
> 3. Equal sharing - twenty-five percent (25%). (Emphasis supplied)

---

[59] Rep. Act No. 7916 (1995), sec. 3.

Based on these provisions, the fiscal incentives and the 5% preferential tax rate are available only to businesses operating within the Ecozone.[60] A business is considered in operation when it starts entering into commercial transactions that are not merely incidental to but are related to the purposes of the business. It is similar to the definition of "doing business," as applied in actions involving the right of foreign corporations to maintain court actions. In *Mentholatum Co. Inc., et al. v. Mangaliman, et al.*,[61] this court said that the terms "doing" or "engaging in" or "transacting" business":

> . . . impl[y] a continuity of commercial dealings and arrangements, and contemplates, to that extent, the performance of acts or works or the exercise of some of the functions normally incident to, and in progressive prosecution of, the purpose and object of its organization.[62]

Petitioner never started its operations since its registration on June 29, 1998[63] because of the Asian financial crisis.[64] Petitioner admitted this.[65] Therefore, it cannot avail the incentives provided under Republic Act No. 7916. It is not entitled to the preferential tax rate of 5% on gross income in lieu of all taxes. Because petitioner is not entitled to a preferential rate, it is subject to ordinary tax rates under the National Internal Revenue Code of 1997.

III
Imposition of capital gains tax

The Court of Tax Appeals found that petitioner's sale of its properties is subject to capital gains tax.

For petitioner's properties to be subjected to capital gains tax, the properties must form part of petitioner's capital assets.

Section 39(A)(1) of the National Internal Revenue Code of 1997 defines "capital assets":

> **SEC. 39. Capital Gains and Losses. -**
>
> **(A) Definitions.** - As used in this Title -
>
> **(1) Capital Assets.** - the term 'capital assets' means property held by the taxpayer (whether or not connected with his trade or

---

60 Rep. Act No. 7916 (1995), secs. 23–24.
61 72 Phil. 524 (1941) [Per J. Laurel, En Banc].
62 Id. at 528–529.
63 *Rollo*, p. 8.
64 Id. at 35.
65 Id. at 62.

> business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, or property *used* in the trade or business, of a character which is subject to the allowance for depreciation provided in Subsection (F) of Section 34; or real property *used* in trade or business of the taxpayer. (Emphasis supplied)

Thus, "capital assets" refers to taxpayer's property that is NOT any of the following:

1. Stock in trade;
2. Property that should be included in the taxpayer's inventory at the close of the taxable year;
3. Property held for sale in the ordinary course of the taxpayer's business;
4. Depreciable property used in the trade or business; and
5. Real property used in the trade or business.

The properties involved in this case include petitioner's buildings, equipment, and machineries. They are not among the exclusions enumerated in Section 39(A)(1) of the National Internal Revenue Code of 1997. None of the properties were used in petitioner's trade or ordinary course of business because petitioner never commenced operations. They were not part of the inventory. None of them were stocks in trade. Based on the definition of capital assets under Section 39 of the National Internal Revenue Code of 1997, they are capital assets.

Respondent insists that since petitioner's machineries and equipment are classified as capital assets, their sales should be subject to capital gains tax. Respondent is mistaken.

In *Commissioner of Internal Revenue v. Fortune Tobacco Corporation,*[66] this court said:

> The rule in the interpretation of tax laws is that a statute will not be construed as imposing a tax unless it does so clearly, expressly, and unambiguously. A tax cannot be imposed without clear and express words for that purpose. Accordingly, the general rule of requiring adherence to the letter in construing statutes applies with peculiar strictness to tax laws and the provisions of a taxing act are not to be extended by implication. In answering the question of who is subject to tax statutes, it is basic that in case of doubt, such statutes are to be construed most strongly against the government and in favor of the subjects or citizens because burdens are

[66] 581 Phil. 146 (2008) [Per J. Tinga, Second Division].

> not to be imposed nor presumed to be imposed beyond what statutes expressly and clearly import. As burdens, taxes should not be unduly exacted nor assumed beyond the plain meaning of the tax laws.[67] (Citations omitted)

Capital gains of individuals and corporations from the sale of real properties are taxed differently.

Individuals are taxed on capital gains from sale of all real properties located in the Philippines and classified as capital assets. Thus:

> **SEC. 24. Income Tax Rates.**
>
> . . . .
>
> (D) Capital Gains from Sale of Real Property. –
>
> > (1) In General. - The provisions of Section 39(B) notwithstanding, a final tax of six percent (6%) based on the gross selling price or current fair market value as determined in accordance with Section 6(E) of this Code, whichever is higher, is hereby imposed upon *capital gains presumed to have been realized from the sale, exchange, or other disposition of real property located in the Philippines, classified as capital assets*, including pacto de retro sales and other forms of conditional sales, by individuals, including estates and trusts: Provided, That the tax liability, if any, on gains from sales or other dispositions of real property to the government or any of its political subdivisions or agencies or to government-owned or controlled corporations shall be determined either under Section 24 (A) or under this Subsection, at the option of the taxpayer.[68] (Emphasis supplied)

For corporations, the National Internal Revenue Code of 1997 treats the sale of land and buildings, and the sale of machineries and equipment, differently. Domestic corporations are imposed a 6% capital gains tax only on the presumed gain realized from the sale of lands and/or buildings. The National Internal Revenue Code of 1997 does not impose the 6% capital gains tax on the gains realized from the sale of machineries and equipment. Section 27(D)(5) of the National Internal Revenue Code of 1997 provides:

> **SEC. 27. Rates of Income tax on Domestic Corporations. -**
>
> . . . .
>
> (D) Rates of Tax on Certain Passive Incomes. -

---

67 Id. at 168.

68 TAX CODE, sec. 24(D)(1).

. . . .

> (5) Capital Gains Realized from the Sale, Exchange or Disposition of Lands and/or Buildings. - A final tax of six percent (6%) is hereby imposed *on the gain presumed to have been realized on the sale, exchange or disposition of lands and/or buildings* which are not actually used in the business of a corporation and are treated as capital assets, based on the gross selling price of fair market value as determined in accordance with Section 6(E) of this Code, whichever is higher, of such lands and/or buildings. (Emphasis supplied)

Therefore, only the presumed gain from the sale of petitioner's land and/or building may be subjected to the 6% capital gains tax. The income from the sale of petitioner's machineries and equipment is subject to the provisions on normal corporate income tax.

To determine, therefore, if petitioner is entitled to refund, the amount of capital gains tax for the sold land and/or building of petitioner and the amount of corporate income tax for the sale of petitioner's machineries and equipment should be deducted from the total final tax paid.

Petitioner indicated, however, in its March 1, 2001 income tax return for the 11-month period ending on November 30, 2000 that it suffered a net loss of □2,233,464,538.00.[69] This declaration was made under the pain of perjury. Section 267 of the National Internal Revenue Code of 1997 provides:

> **SEC. 267. Declaration under Penalties of Perjury. -** Any declaration, return and other statement required under this Code, shall, in lieu of an oath, contain a written statement that they are made under the penalties of perjury. Any person who willfully files a declaration, return or statement containing information which is not true and correct as to every material matter shall, upon conviction, be subject to the penalties prescribed for perjury under the Revised Penal Code.

Moreover, Rule 131, Section 3(ff) of the Rules of Court provides for the presumption that the law has been obeyed unless contradicted or overcome by other evidence, thus:

> SEC. 3. *Disputable presumptions.*— The following presumptions are satisfactory if uncontradicted, but may be contradicted and overcome by other evidence:
>
> . . . .

---

[69] *Rollo*, p. 9.

> (ff) That the law has been obeyed;

The BIR did not make a deficiency assessment for this declaration. Neither did the BIR dispute this statement in its pleadings filed before this court. There is, therefore, no reason to doubt the truth that petitioner indeed suffered a net loss in 2000.

Since petitioner had not started its operations, it was also not subject to the minimum corporate income tax of 2% on gross income.[70] Therefore, petitioner is not liable for any income tax.

IV
Prescription

Section 203 of the National Internal Revenue Code of 1997 provides that as a general rule, the BIR has three (3) years from the last day prescribed by law for the filing of a return to make an assessment. If the return is filed beyond the last day prescribed by law for filing, the three-year period shall run from the actual date of filing. Thus:

> **SEC. 203. Period of Limitation Upon Assessment and Collection**. - Except as provided in Section 222, internal revenue taxes shall be assessed within three (3) years after the last day prescribed by law for the filing of the return, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period: Provided, That in a case where a return is filed beyond the period prescribed by law, the three (3)-year period shall be counted from the day the return was filed. For purposes of this Section, a return filed before the last day prescribed by law for the filing thereof shall be considered as filed on such last day.

This court said that the prescriptive period to make an assessment of internal revenue taxes is provided "primarily to safeguard the interests of taxpayers from unreasonable investigation."[71]

This court explained in *Commissioner of Internal Revenue v. FMF Development Corporation*[72] the reason behind the provisions on prescriptive periods for tax assessments:

> Accordingly, the government must assess internal revenue taxes on

---

70 TAX CODE, sec. (E)(1).

71 *Commissioner of Internal Revenue v. FMF Development Corporation*, 579 Phil. 174, 183 (2008) [Per J. Quisumbing, Second Division].

72 579 Phil. 174 (2008) [Per J. Quisumbing, Second Division].

> time so as not to extend indefinitely the period of assessment and deprive the taxpayer of the assurance that it will no longer be subjected to further investigation for taxes after the expiration of reasonable period of time.[73]

Rules derogating taxpayers' right against prolonged and unscrupulous investigations are strictly construed against the government.[74]

> [T]he law on prescription should be interpreted in a way conducive to bringing about the beneficent purpose of affording protection to the taxpayer within the contemplation of the Commission which recommended the approval of the law. To the Government, its tax officers are obliged to act promptly in the making of assessment so that taxpayers, after the lapse of the period of prescription, would have a feeling of security against unscrupulous tax agents who will always try to find an excuse to inspect the books of taxpayers, not to determine the latter's real liability, but to take advantage of a possible opportunity to harass even law-abiding businessmen. Without such legal defense, taxpayers would be open season to harassment by unscrupulous tax agents.[75]

Moreover, in *Commissioner of Internal Revenue v. BF Goodrich Phils.*:[76]

> For the purpose of safeguarding taxpayers from any unreasonable examination, investigation or assessment, our tax law provides a statute of limitations in the collection of taxes. Thus, the law on prescription, being a remedial measure, should be liberally construed in order to afford such protection. As a corollary, the exceptions to the law on prescription should perforce be strictly construed[.]
>
> . . . .
>
> . . . . Such instances of negligence or oversight on the part of the BIR cannot prejudice taxpayers, considering that the prescriptive period was precisely intended to give them peace of mind.[77] (Citation omitted)

The BIR had three years from the filing of petitioner's final tax return in 2000 to assess petitioner's taxes. Nothing stopped the BIR from making the correct assessment. The elevation of the refund claim with the Court of Tax Appeals was not a bar against the BIR's exercise of its assessment powers.

---

73 Id. at 183, *citing Philippine Journalists, Inc. v. Commissioner of Internal Revenue*, 488 Phil. 218, 229–230 (2004) [Per J. Ynares-Santiago, First Division].

74 *Commissioner of Internal Revenue v. FMF Development Corporation*, 579 Phil. 174, 185 (2008) [Per J. Quisumbing, Second Division].

75 Id. at 186, *citing Republic v. Ablaza*, 108 Phil. 1105, 1108 (1960) [Per J. Labrador, En Banc].

76 363 Phil. 169 (1999) [Per J. Panganiban, Third Division].

77 Id. at 178–180.

The BIR, however, did not initiate any assessment for deficiency capital gains tax.[78] Since more than a decade have lapsed from the filing of petitioner's return, the BIR can no longer assess petitioner for deficiency capital gains taxes, if petitioner is later found to have capital gains tax liabilities in excess of the amount claimed for refund.

The Court of Tax Appeals should not be expected to perform the BIR's duties of assessing and collecting taxes whenever the BIR, through neglect or oversight, fails to do so within the prescriptive period allowed by law.

WHEREFORE, the Court of Tax Appeals' November 3, 2006 decision is **SET ASIDE.** The Bureau of Internal Revenue is ordered to refund petitioner SMI-Ed Philippines Technology, Inc. the amount of 5% final tax paid to the BIR, less the 6% capital gains tax on the sale of petitioner SMI-Ed Philippines Technology, Inc.'s land and building. In view of the lapse of the prescriptive period for assessment, any capital gains tax accrued from the sale of its land and building that is in excess of the 5% final tax paid to the Bureau of Internal Revenue may no longer be recovered from petitioner SMI-Ed Philippines Technology, Inc.

SO ORDERED.

MARVIC M.V.F. LEONEN
Associate Justice

WE CONCUR:

ANTONIO T. CARPIO
Associate Justice
Chairperson

ARTURO D. BRION
Associate Justice

MARIANO C. DEL CASTILLO
Associate Justice

JOSE CATRAL MENDOZA
Associate Justice

---

78 *Rollo*, p. 250.

CERTIFICATION

Pursuant to Section 13, Article VIII of the Constitution, I certify that the conclusions in the above Decision had been reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

ANTONIO T. CARPIO
Acting Chief Justice