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THIRD DIVISION

[G.R. No. 107434. October 10, 1997]

CITIBANK, N. A., *petitioner, vs.* **COURT OF APPEALS and COMMISSIONER OF INTERNAL REVENUE,** *respondents.*

SYNOPSIS

In 1979 and 1980 petitioner Citibank N.A.'s tenants withheld and paid to the Bureau of Internal Revenue taxes on rents to Citibank pursuant to Section 1 (c) of the Expanded Withholding Tax Regulations (BIR Revenue Regulations No. 13-78, as amended). Citibank did not include the amounts withheld under the aforementioned regulations in its corporate income tax returns for the year 1979 for the reason that the year's operation resulted in a loss. The taxes withheld were not included as tax credits. Citibank submitted its claim for refund and thereafter filed a petition for review with the Court of Tax Appeals concerning the subject claim. The Court of Tax Appeals granted the refund to the petitioner. The Commissioner of Internal Revenue appealed to the Court of Appeals. The appellate court reversed the ruling of the Court of Tax Appeals on the ground that the refund sought for by petitioner did not involve illegally or erroneously collected taxes. Respondent court denied the motion for reconsideration of petitioner bank. Hence, the present petition.

The Supreme Court ruled that the withheld amounts equivalent to five percent of the gross rental and remitted to the BIR are considered creditable withholding taxes under Section 53-f of the National Internal Revenue Code, *i.e.*, creditable against the income tax liability for that year. The taxes withheld are in the nature of payment by a taxpayer in order to extinguish his possible tax obligations. The payments of the withholding taxes for 1979 and 1980 were creditable to the income tax liability, if any, of petitioner-bank, determined after the filing by the petitioner-bank of corporate income tax returns on April 15, 1980 and April 15, 1981. As petitioner posted losses in its 1979 and 1980 returns, it was not liable for any income taxes. Consequently, the taxes withheld during the course of the taxable year, while collected legally under the aforesaid revenue regulation, became

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untenable and took on the nature of erroneously collected taxes at the end of the taxable year.

Petition granted.

SYLLABUS

1. **TAXATION; NATIONAL INTERNAL REVENUE CODE; RECOVERY OF TAX ERRONEOUSLY OR ILLEGALLY COLLECTED; INCOME TAXES REMITTED PARTIALLY ON A PERIODIC OR QUARTERLY BASIS SHOULD BE CREDITED OR REFUNDED TO THE TAXPAYER'S FINAL ADJUSTED RETURNS, NOT ON SUCH PERIODIC OR QUARTERLY BASIS.**— We have already ruled that income taxes remitted partially on a periodic or quarterly basis should be credited or refunded to the taxpayer on the basis of the taxpayer's final adjusted returns, not on such periodic or quarterly basis. In the present case, there is no question that the taxes were withheld in accordance with Section 1(c), Rev. Reg. No. 13-78. In that sense, it can be said that they were withheld legally by the tenants. However, the annual income tax returns of petitioner-bank for tax years 1979 and 1980 undisputedly reflected the net losses it suffered. The question arises: whether the taxes withheld remained legal and correct at the end of each taxable year. We hold in the negative.

2. **ID.; ID.; ID.; ID.; THE TAXES WITHHELD ARE IN THE NATURE OF PAYMENT BY A TAXPAYER IN ORDER TO EXTINGUISH HIS POSSIBLE TAX OBLIGATION; THEY ARE INSTALLMENTS ON THE ANNUAL TAX WHICH MAY BE DUE AT THE END OF THE TAXABLE YEAR.**— The withheld amounts equivalent to five percent of the gross rental are remitted to the BIR and are considered creditable withholding taxes under Section 53-f, *i.e.*, creditable against income tax liability for that year. The taxes withheld, as ruled in *Gibbs vs. Commissioner of Internal Revenue*, 15 SCRA 318, 325, Nov. 29, 1965 are in the nature of payment by a taxpayer in order to extinguish his possible tax obligation. They are installments on the annual tax which may be due at the end of the taxable year.

3. **ID.; ID.; ID.; ID.; LIKE THE CORPORATE QUARTERLY INCOME TAX, CREDITABLE WITHHOLDING TAXES ARE SUBJECT TO ADJUSTMENT UPON DETER-**

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MINATION OF THE CORRECT INCOME TAX LIABILITY AFTER THE FILING OF THE CORPORATE INCOME TAX RETURN AT THE END OF THE TAXABLE YEAR.— Petitioner's lessees withheld and remitted to the BIR the amounts now claimed as tax refunds. That they were withheld and remitted pursuant to Rev. Reg. No. 13-78 does not derogate from the fact that they were merely partial payments of probable taxes. Like the corporate quarterly income tax, creditable withholding taxes are subject to adjustment upon determination of the correct income tax liability after the filing of the corporate income tax return, as at the end of the taxable year. This final determination of the corporate income tax liability is provided in Section 69, NIRC. The taxes thus withheld and remitted are *provisional* in nature. We repeat: five per cent of the rental income withheld and remitted to the BIR pursuant to Rev. Reg. No. 13-78 is, unlike the withholding of final taxes on passive incomes, a *creditable* withholding tax; that is, creditable against income tax liability if any, for that taxable year.

4. **ID.; ID.; ID.; ID.; CASE AT BAR; THE TAXES WITHHELD FOR 1979 AND 1980, WHILE COLLECTED LEGALLY UNDER REVENUE REGULATION 12-94, BECAME UNTENABLE AND TOOK ON THE NATURE OF ERRONEOUSLY COLLECTED TAXES AT THE END OF THE TAXABLE YEAR.**— In this case, the payments of the withholding taxes for 1979 and 1980 were creditable to the income tax liability, if any, of petitioner-bank, determined after the filing of the corporate income tax returns on April 15, 1980 and April 15, 1981. As petitioner posted net losses in its 1979 and 1980 returns, it was not liable for any income taxes. Consequently and clearly, the taxes withheld during the course of the taxable year, while collected legally under the aforesaid revenue regulation, became untenable and took on the nature of erroneously collected taxes at the end of the taxable year.

5. **ID.; ID.; TAX REFUND; CLAIMANT HAS THE BURDEN OF PROOF TO ESTABLISH THE FACTUAL BASIS OF CLAIM FOR TAX CREDIT OR REFUND.**— In general, there is no disagreement that a claimant has the burden of proof to establish the factual basis of his or her claim for tax credit or refund. Tax refunds, like tax exemptions, are construed strictly against the taxpayer. The mechanics of a tax refund is provided in Rev. Reg. No. 13-78. A refund claimant is required to prove

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the inclusion of the income payments which were the basis of the withholding taxes and the fact of withholding. However, detailed proof of the truthfulness of each and every item in the income tax return is not required. That function is lodged in the Commissioner of Internal Revenue by the NIRC which requires the commissioner to assess internal revenue taxes within three years after the last day prescribed by law for the filing of the return.

6. **ID.; ID.; PRESCRIPTION OF ACTION; TO EXPECT PETITIONER TO HAVE ITS BOOKS AND RECORDS ON HAND DURING THE APPEAL WAS OBVIOUSLY UNREASONABLE AND VIOLATIVE OF SECTION 235 IN RELATION TO SECTION 203 OF THE TAX CODE.—** In the CTA (Court of Tax Appeal), Respondent Commissioner's refusal to refund was based on the argument that the claim filed on October 31, 1981 was time-barred. It bears stressing that the issue of prescription was not raised in the appeal before us. The issue of operational losses was not raised until the appeal before Respondent Court was filed on February 5, 1992. By such time, at least a decade had already passed since the pertinent books and accounting records of petitioner-bank were closed. Section 235 of the Tax Code requires the preservation of the books of account and records only "for a period beginning from the last entry in each book until the last day prescribed by Section 203." Section 203 provides that internal revenue taxes shall be assessed within three years after the last day prescribed by law for the filing of the return, and no proceeding in Court without an assessment for the collection of such taxes shall begin after the expiration of such period. To expect petitioner to have its books and records on hand during the appeal was obviously unreasonable and violative of Section 235 in relation to Section 203 of the Tax Code.

7. **CIVIL CODE; PRINCIPLE OF *SOLUTIO INDEBITI*; PRINCIPLE THAT NO ONE, NOT EVEN THE STATE, SHALL ENRICH ONESELF AT THE EXPENSE OF ANOTHER; SIMPLE JUSTICE REQUIRES THE SPEEDY REFUND OF WRONGLY HELD TAXES.—** Worth emphasizing are these uncontested facts: (1) the amounts withheld were actually remitted to the BIR and (2) the final adjusted returns — which the BIR did not question — showed that, for

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1979 and 1980, no income taxes from petitioner were due. Hence, under the principle of *solutio indebiti* provided in Art. 2154, Civil Code, the BIR received something when "there [was] no right to demand it," and thus "the obligation to return arises." Heavily militating against Respondent Commissioner is the ancient principle that no one, not even the state, shall enrich oneself at the expense of another. Indeed, simple justice requires the speedy refund of the wrongly held taxes.

APPEARANCES OF COUNSEL

Romulo, Mabanta, Buenaventura, Sayoc & De Los Angeles for petitioner.

The Solicitor General for respondents.

DECISION

PANGANIBAN, *J.*:

The law requires a lessee to withhold and remit to the Bureau of Internal Revenue (BIR) five percent (5%) of the rental due the lessor, by way of advance payment of the latter's income tax liability. Is the lessor entitled to a refund of such withheld amount after it is determined that the lessor was not, in fact, liable for any income tax at all because its annual operation resulted in a net loss as shown in its income tax return filed at the end of the taxable year?

This is the question raised in this petition for review on *certiorari* of the Court of Appeals[1] Decision[2] promulgated on May 27, 1992 and Resolution[3] promulgated on October 5, 1992 in CA-G.R. No. SP-26555, reversing the decision of the Court of Tax Appeals which allowed the tax refund.

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[1] Special Tenth Division consisting of *JJ.* Fidel P. Purisima, chairman and *ponente,* Minerva P. Gonzaga-Reyes and Fermin A. Martin, Jr.

[2] *Rollo,* pp. 24-28.

[3] *Rollo,* pp. 21-22.

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The Facts

The facts, as found by Respondent Court, are undisputed.[4]

"From the pleadings and supporting papers on hand, it can be gathered that Citibank N.A. Philippine Branch (CITIBANK) is a foreign corporation doing business in the Philippines. In 1979 and 1980, its tenants withheld and paid to the Bureau of Internal Revenue the following taxes on rents due to Citibank, pursuant to Section 1(c) of the Expanded Withholding Tax Regulations (BIR Revenue Regulations No. 13-78, as amended), to wit:

1979	
First quarter	₱60,690.97
Second quarter	69,897.08
Third quarter	69,160.89
Fourth quarter	70,160.56
	₱270,160.56
1980	
First quarter	₱78,370.22
Second quarter	69,049.37
Third quarter	79,139.60
Fourth quarter	72,270.10
	₱298,829.29

On April 15, 1980, Citibank filed its corporate income tax returns for the year ended December 31, 1979 (Exh. "E:), showing a net loss of ₱74,854,916.00 and its tax credits totalled ₱6,257,780.00, even without including the amounts withheld on rental income under the Expanded Withholding Tax System, the same not having been utilized or applied for the reason that the year's operation resulted in a loss. (Exh. "E-1 & E-2"). The taxes thus withheld by the tenants from rentals paid to Citibank in 1979 were not included as tax credits although a rental income amounting to ₱7,796,811.00 was included in its income declared for the year ended December 31, 1979 (Exhs. "E-3" & "E-4").

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[4] *Rollo*, pp. 24-26.

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For the year ended December 31, 1980, Citibank's corporate income tax returns (Exh. "EC"), filed on April 15, 1981, showed a net loss of ₱77,071,790.00 for income tax purposes. Its available tax credit (refundable) at the end of 1980 amounting to ₱11,532,855.00 (Exh. "BC-1" & "BC-2") was not utilized or applied. The said available tax credits did not include the amounts withheld by Citibank's tenants from rental payments in 1980 but the rental payments for that year were declared as part of its gross income included in its annual income tax returns (Exh. "BC-3").

On October 31, 1981, Citibank submitted its claim for refund of the aforesaid amounts of ₱270,160.56 and ₱298,829, respectively, or a total of ₱568,989.85; and on October 12, 1981 filed a petition for review with the Court of Tax Appeals concerning subject claim for tax refund, docketed as CTA Case No. 3378.[5]

On August 30, 1981, the Court of Tax Appeals adjudged Citibank's entitlement to the tax refund sought for, representing the 5% tax withheld and paid on Citibank's rental income for 1979 and 1980. x x x."

In its decision[6] granting a refund to petitioner,[7] the Court of Tax Appeals rejected Respondent Commissioner's argument that the claim was not seasonably filed:

"WHEREFORE, respondent is hereby ordered to grant the refund of the amount sought by the petitioner. No costs."

Not satisfied, the Commissioner appealed to the Court of Appeals. In due course, Respondent Court issued the assailed Decision and Resolution, ruling that the five percent tax withheld by tenants from the rental income of Citibank for the years 1979 and 1980 was in accordance with Section 1(c) of the Expanded Withholding Tax Regulations (BIR Revenue Regulation No. 13-78, as amended) and did not involve illegally

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[5] Docketed as C.T.A. Case No. 3378.

[6] Penned by Presiding Judge Alex Z. Reyes and concurred in by Associate Judges Constante C. Roaquin and Ernesto D. Acosta.

[7] CA *rollo*, pp. 29-31.

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or erroneously collected taxes. The dispositive portion of the Decision reads:[8]

"WHEREFORE, the appealed judgment of August 30, 1991, adjudging Citibank, N.A., Philippine Branch, entitled to a tax refund/credit in the amount of ₱569,989.85, representing the 5% withheld tax on Citibank's rental income for the taxable years 1979 and 1980 is hereby REVERSED. No pronouncement as to costs."

Respondent Court denied the motion for reconsideration of the petitioner-bank in the assailed Resolution, the dispositive portion of which reads:[9]

"WHEREFORE, for want of merit, the motion for reconsideration, dated June 19, 1992, of respondent Citibank, N.A. is hereby DENIED.

SO ORDERED."

Hence, this petition under Rule 45 of the Rules of Court.

The Issues

The appellate court ruled that it was not enough for petitioner to show its lack of income tax liability against which the five percent withholding tax could be credited. Petitioner should have also shown that the withholding tax was illegally or erroneously collected and remitted by the tenants. On the other hand, petitioner counters that Respondent Court failed to grasp "two fundamental concepts in the present income tax system, namely: (1) the yearly computation of the corporate income tax and (2) the nature of the creditable withholding tax."

In the main, petitioner thus raises the following issues: (1) For creditable withholding tax to be refundable, when should the illegality or error in its assessment or collection be reckoned: at the time of withholding or at the end of the taxable year? (2) Where the income tax returns show that no income tax is payable to the government, is a *creditable* withholding tax, as

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[8] *Rollo*, pp. 24-28.

[9] *Rollo*, pp. 21-22.

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contradistinguished from a *final* tax, refundable (or creditable) at the end of the taxable year?

The Court's Ruling

The petition is meritorious.

First Issue: Determination of the Illegality or Error in Assessment or Collection

Tax refunds are allowed under Section 230 of the National Internal Revenue Code:

"SEC. 230. *Recovery of tax erroneously or illegally collected.*— No suit or proceeding shall be maintained in any court for the recovery of any national internal revenue tax hereafter alleged to have been erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority or of any sum alleged to have been excessive or in any manner wrongfully collected, until a claim for refund or credit has been duly filed with the Commissioner; but such suit or proceeding may be maintained, whether or not such tax, penalty, or sum has been paid under protest or duress.

In any case, no such suit or proceeding shall be begun after the expiration of two years from the date of payment of the tax or penalty regardless of any supervening cause that may arise after payment: *Provided, however,* That the Commissioner may, even without a written claim therefor, refund or credit any tax, where on the face of the return upon which payment was made, such payment appears clearly to have been erroneously paid."

Petitioner maintains that it is entitled to a refund of the five percent creditable withholding tax in 1979 and 1980, since its operations resulted in a net loss and thus did not have any income tax liability for such years. Respondent Court refused to allow the claim for refund for the reason that the taxes were "not illegally or erroneously collected:"[10]

"It is decisively clear that the instant claim for tax refund under scrutiny does not involve illegally or erroneously collected taxes. It involves the 5% tax withheld by tenants from the rental income of

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[10] *Rollo*, pp. 26-27.

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Citibank for the years 1979 and 1980, in accordance with Section 1(c) of the Expanded Withholding Tax Regulations (BIR Revenue Regulation No. 13-78 as amended) x x x.

It is thus evident that the tenants or lessee of Citibank were required by law to withhold and pay to BIR 5% of their rental and, therefore, such withholding taxes were not illegally or erroneously collected. It was the burden of Citibank to prove that the taxes it asked to be refunded were illegally or erroneously collected; an *onus probandi* Citibank utterly failed to discharge."

We disagree with the Court of Appeals. In several cases, we have already ruled that income taxes remitted partially on a periodic or quarterly basis should be credited or refunded to the taxpayer on the basis of the taxpayer's final adjusted returns, not on such periodic or quarterly basis.[11] For instance, in the recent case of *Commissioner of Internal Revenue vs. Philippine American Life Insurance Co.,*[12] the Court held:

"x x x When applied to taxpayers filing income tax returns on a quarterly basis, the date of payment mentioned in Section 292 (now Section 230) must be deemed to be qualified by Sections 68 and 69 of the present Tax Code x x x.

It may be observed that although quarterly taxes due are required to be paid within 60 days from the close of each quarter, the fact that the amount shall be deducted from the tax due for the succeeding quarter shows that until a final adjustment return shall have been filed, the taxes paid in the preceding quarters are merely partial taxes due from a corporation. Neither amount can serve as the final figure to quantify what is due the government nor what should be refunded to the corporation.

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[11] *Collector vs. Antonio Prieto,* 2 SCRA 1007, 1016-1017, August 29, 1961; *Gibbs vs. Commissioner of Internal Revenue,* 15 SCRA 318, 325, November 29, 1965; *Commissioner of Internal Revenue vs. Carlos Palanca,* 18 SCRA 496, 504, October 29, 1966; *ACCRA Investments Corporation vs. Court of Appeals,* 204 SCRA 957, 963-964, December 20, 1991; *Commissioner of Internal Revenue vs. TMX Sales, Inc.,* 205 SCRA 184, 192, January 15, 1992; and *Commissioner of Internal Revenue vs. Philippine American Life Insurance Co.,* 244 SCRA 446, 453, May 29, 1995.

[12] *Supra,* pp. 452- 453, per Romero, *J.*

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This interpretation may be gleaned from the last paragraph of Section 69 of the Tax Code which provides that the refundable amount, in case a refund is due a corporation, is that amount which is shown on its final adjustment return and not on its quarterly returns.

x x x x x x x x x

Clearly the prescriptive period of two years should commence to run only from the time that the refund is ascertained, which can only be determined after a final adjustment return is accomplished. Private respondent being a corporation, Section 292 (now Section 230) cannot serve as the sole basis for determining the two-year prescriptive period for refunds. x x x x."

In the present case, there is no question that the taxes were withheld in accordance with Section 1(c), Rev. Reg. No. 13-78. In that sense, it can be said that they were withheld legally by the tenants. However, the annual income tax returns of petitioner-bank for tax years 1979 and 1980 undisputedly reflected the net losses it suffered. The question arises: whether the taxes withheld remained legal and correct at the end of each taxable year. We hold in the negative.

The withholding tax system was devised for two main reasons: *first,* to provide the taxpayer a convenient manner to meet his probable income tax liability; and *second,* to ensure the collection of the income tax which could otherwise be lost or substantially reduced through failure to file the corresponding returns.[13] To these, a third reason may be added: to improve the government's cash flow. Under Section 53 a-f of the tax code which was in effect at the time this case ripened, withholding of tax at source was mandated in cases of: (a) tax free covenant bonds, (b) payments of interest, dividends, rents, royalties, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, or other fixed or determinable annual, periodical, or casual gains, profits and income, and capital gains of non-resident aliens and foreign corporations; (c) dividends from a

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[13] Cesar.C. Rey, *Tax Code Annotated,* p. 243 citing the explanatory note to H. Bill No. 1127; and *Commissioner of Internal Revenue vs. Malayan Ins. Co., Inc.,* 21 SCRA 944, 949, November 18, 1967.

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domestic corporation and royalties received by resident individuals and corporation; (d) certain dividends; (e) interest on bank deposit; and (f) other items of income payable to resident individuals or corporations. Section 53-f was amended by Presidential Decree No. 1351, delegating to the Secretary of Finance the power to require the withholding of a tax, as follows:

"Section 1. Section 53(f) of the National Internal Revenue Code of 1997 is hereby amended to read as follows:

'(f) The Secretary of Finance may, upon recommendation of the Commissioner of Internal Revenue, require also the withholding of a tax on the same items of income payable to persons (natural or juridical) residing in the Philippines by the same persons mentioned in paragraph (b) (1) of this Section at the rate of not less than 2-1/2% but not more than 35% thereof which shall be credited against the income tax liability of the taxpayer for the taxable year.'"

Pursuant to said P.D. No. 1351 and in accordance with Section 4 in relation to Section 326[14] of the National Internal Revenue Code, the Commissioner promulgated on September 7, 1978, Revenue Regulations No. 13-78 to implement the withholding of creditable income taxes from certain types of income. Rev. Reg. No. 13-78 requires that a certain percentage of income be deducted and withheld by a payor, who is constituted as the withholding agent, and paid to the revenue district officer or BIR collection agent. Section 1 of this revenue regulation provides:

"Section 1. *Income payments subject to withholding tax and rates prescribed therein.* — Except as herein otherwise provided, there shall be withheld a creditable income tax at the rates herein specified for each class of payee from the following items of income payments to persons residing in the Philippines:

(a) x x x x x x x x x

(b) x x x x x x x x x

(c) *Rentals.* — When the gross rental or other payment required to be made as a condition to the continued use or possession of property,

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[14] Now, Section 4(j), NIRC.

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whether real or personal, to which the payor or obligor has not taken or is not taking title or in which he has no equity, exceeds five hundred pesos (₱500.00) — five per centum (5%).

x x x x x x x x x"

Under this system, income is viewed as a flow[15] and is measured over a period of time known as an "accounting period." An accounting period covers twelve months, subdivided into four equal segments known as "quarters." Income realized within the taxpayer's annual accounting period (fiscal or calendar year) becomes the basis for the computation of the gross income and the tax liability.[16]

The same basic principles apply under the prevailing tax laws. Under the present tax code, the types of income subject to withholding tax in Section 53, now Section 50, is simplified into three categories: (a) withholding of final tax on certain incomes; (b) withholding of creditable tax at source; and (c) tax free covenant bonds.

Accordingly, the withheld amounts equivalent to five percent of the gross rental are remitted to the BIR and are considered creditable withholding taxes under Section 53-f, *i.e.*, creditable against income tax liability for that year. The taxes withheld, as ruled in *Gibbs vs. Commissioner of Internal Revenue*,[17] are in the nature of payment by a taxpayer in order to extinguish his possible tax obligation. They are installments on the annual tax which may be due at the end of the taxable year.[18]

In this case, petitioner's lessees withheld and remitted to the BIR the amounts now claimed as tax refunds. That they were withheld and remitted pursuant to Rev. Reg. No. 13-78

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[15] *Madrigal vs. Rafferty,* 38 Phil. 414, 418 (1918).

[16] Section 37, NIRC.

[17] 15 SCRA 318, 325, November 29, 1965, per Regala, *J.*

[18] *Commissioner of Internal Revenue vs. TMX Sales, Inc., supra,* pp. 191-192; *Collector vs. Prieto, supra;* and *ACCRA Investments Corp. vs. Commissioner, supra.*

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does not derogate from the fact that they were merely partial payments of probable taxes. Like the corporate quarterly income tax, creditable withholding taxes are subject to adjustment upon determination of the correct income tax liability after the filing of the corporate income tax return, as at the end of the taxable year. This final determination of the corporate income tax liability is provided in Section 69, NIRC:

"SEC. 69. Final Adjustment Return. - Every corporation liable to tax under Section 24 shall file a final adjustment return covering the total taxable income for the preceding calendar or fiscal year. If the sum of the quarterly tax payments made during the said taxable year is not equal to the total tax due on the entire taxable net income of that year the corporation shall either:

(a) Pay the excess tax still due; or

(b) Be refunded the excess amount paid, as the case may be.

In case the corporation is entitled to a refund of the excess estimated quarterly income taxes paid, the refundable amount shown on its final adjustment return may be credited against the estimated quarterly income tax liabilities for the taxable quarters of the succeeding taxable year."

The taxes thus withheld and remitted are *provisional* in nature.[19] We repeat: five per cent of the rental income withheld and remitted to the BIR pursuant to Rev. Reg. No. 13-78 is, unlike the withholding of final taxes on passive incomes, a creditable withholding tax; that is, creditable against income tax liability if any, for that taxable year.

In *Commissioner of Internal Revenue vs. TMX Sales, Inc.*,[20] this Court ruled that the payments of quarterly income taxes (per Section 68, NIRC) should be considered mere installments on the annual tax due. These quarterly tax payments, which are computed based on the cumulative figures of gross receipts and deductions in order to arrive at a net taxable income, should

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[19] From the concurring opinion of J. Jose C. Vitug in *Commissioner of Internal Revenue vs. Philippine American Life Insurance Co., supra.*

[20] 205 SCRA 184, January 15, 1992.

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be treated as advances or portions of the annual income tax due, to be adjusted at the end of the calendar or fiscal year. The same holds true in the case of the withholding of creditable tax at source. Withholding taxes are "deposits" which are subject to adjustments at the proper time when the complete tax liability is determined.

In this case, the payments of the withholding taxes for 1979 and 1980 were creditable to the income tax liability, if any, of petitioner-bank, determined after the filing of the corporate income tax returns on April 15, 1980 and April 15, 1981. As petitioner posted net losses in its 1979 and 1980 returns, it was not liable for any income taxes. Consequently and clearly, the taxes withheld during the course of the taxable year, while collected legally under the aforesaid revenue regulation, became untenable and took on the nature of erroneously collected taxes at the end of the taxable year.

Second Issue: *Onus of Disputing a Claim for Refund*

In general, there is no disagreement that a claimant has the burden of proof to establish the factual basis of his or her claim for tax credit or refund.[21] Tax refunds, like tax exemptions, are construed strictly against the taxpayer. The mechanics of a tax refund is provided in Rev. Reg. No. 13-78:

"Section 8. *Claims for tax credit or refund.* - Claims for tax credit or refund of income tax deducted and withheld on income payments shall be given due course only when it is shown on the return that the income payment received was declared as part of the gross income and the fact of withholding is established by a copy of the statement, duly issued by the payor to the payee (BIR Form No. 1743-A) showing the amount paid and the amount of tax withheld therefrom."

A refund claimant is required to prove the inclusion of the income payments which were the basis of the withholding taxes and the fact of withholding. However, detailed proof of the truthfulness of each and every item in the income tax return is

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[21] *Commissioner of Internal Revenue vs. Tokyo Shipping Co., Ltd.*, 244 SCRA 332, 336, May 26, 1995, per Puno, *J.*

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not required. That function is lodged in the commissioner of internal revenue by the NIRC which requires the commissioner to assess internal revenue taxes within three years after the last day prescribed by law for the filing of the return.[22] In *San Carlos Milling Co., Inc. vs. Commissioner of Internal Revenue,*[23] the Court held that the internal revenue branch of government must investigate and confirm the claims for tax refund or credit before taxpayers may avail themselves of this option. The grant of a refund is founded on the assumption that the tax return is valid; that is, the facts stated therein are true and correct.[24] In fact, even without petitioner's tax claim, the commissioner can proceed to examine the books, records of the petitioner-bank, or any data which may be relevant or material in accordance with Section 16 of the present NIRC.

In the case in hand, Respondent Commissioner examined petitioner's income tax returns and presumably found no false declaration in them, because he did not allege any such false declaration before Respondent Court and the Court of Tax Appeals (CTA). In the CTA, Respondent Commissioner's refusal to refund was based on the argument that the claim filed on October 31, 1981 was time-barred. It bears stressing that this issue was not raised in the appeal before us. The issue of operational losses was not raised until the appeal before Respondent Court was filed on February 5, 1992. By such time, at least a decade had already passed since the pertinent books and accounting records of petitioner-bank were closed. Section 235 of the Tax Code requires the preservation of the books of account and records only "for a period beginning from the last entry in each book until the last day prescribed by Section 203." Section 203 provides that internal revenue taxes shall be assessed within three years after the last day prescribed by law for the filing of the return, and no proceeding in Court without an assessment for the collection of such taxes shall

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[22] Section 16 and 203, NIRC.

[23] 228 SCRA 135, 141, November 23, 1993, per Padilla, *J.*

[24] *Commissioner of Internal Revenue vs. Court of Tax Appeals,* 234 SCRA 348, 357, July 21, 1994 per Regalado, *J.*

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begin after the expiration of such period. To expect petitioner to have its books and records on hand during the appeal was obviously unreasonable and violative of Section 235 in relation to Section 203 of the Tax Code.

In addition, the Tax Code has placed several safety measures to prevent falsification of income tax returns which the Court recognized in *Commissioner vs. TMX Sales, Inc.*:[25]

"Furthermore, Section 321 (now Section 232) of the National Internal Revenue Code requires that the books of accounts of companies or persons with gross quarterly sales or earnings exceeding Twenty Five Thousand Pesos (₱25,000.00) be audited and examined yearly by an independent Certified Public Accountant and their income tax returns be accompanied by certified balance sheets, profit and loss statements, schedules listing income producing properties and the corresponding incomes therefrom and other related statements.

It is generally recognized that before an accountant can make a certification on the financial statements or render an auditor's opinion, an audit of the books of accounts has to be conducted in accordance with generally accepted auditing standards.

Since the audit, as required by Section 321 (now Section 232) of the Tax Code is to be conducted yearly, then it is the Final Adjustment Return, where the figures of the gross receipts and deductions have been audited and adjusted, that is truly reflective of the results of the operations of a business enterprise. Thus, it is only when the Adjustment Return covering the whole year is filed that the taxpayer would know whether a tax is still due or a refund can be claimed based on the adjusted and audited figures."

Therefore, the alleged irregularity in the declared operational losses is a matter which must be proven by competent evidence. In resisting the claims of petitioner, Respondent Commissioner set up the defense of the legality of the collection of the creditable withholding tax as well as prescription, instead of presenting an assessment of the proper tax liability of the petitioner. This fact leads us to the conclusion that the income tax returns were accepted as accurate and regular by the BIR.

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[25] *Supra,* per Gutierrez, *J.*

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After this case was filed, the Commissioner clarified on June 27, 1994, the *onus probandi* of a taxpayer claiming refund of overpaid withholding taxes, *inter alia,* in Revenue Regulation No. 12-94, Section 10:

"Section 10. Claim for Tax Credit or Refund.—

(a) Claims for Tax Credit or Refund of income tax deducted and withheld on income payments shall be given due course only when it is shown on the return that the income payment received has been declared as part of the gross income and the fact of withholding is established by a copy of the Withholding Tax Statement duly issued by the payor to the payee showing the amount paid and the amount of tax withheld therefrom.

(b) Excess Credits.— A taxpayer's excess expanded withholding tax credits for the taxable quarter/taxable year shall automatically be allowed as a credit for purposes of filing his income tax return for the taxable quarter/taxable year immediately succeeding the taxable quarter/taxable year in which the aforesaid excess credit arose, provided, however, he submits with his income tax return a copy of his income tax return for the aforesaid previous taxable period showing the amount of his aforementioned excess withholding tax credits.

If the taxpayer, in lieu of the aforesaid automatic application of his excess credit, wants a cash refund or a tax credit certificate for use in payment of his other national internal tax liabilities, he shall make a written request therefor. Upon filing of his request, the taxpayer's income tax return showing the excess expanded withholding tax credits shall be examined. The excess expanded withholding tax, if any, shall be determined and refunded/credited to the taxpayer-applicant. The refund/credit shall be made within a period of sixty (60) days from date of the taxpayer's request provided, however, that the taxpayer-applicant submitted for audit all his pertinent accounting records and that the aforesaid records established the veracity of his claim for a refund/credit of his excess expanded withholding tax credits."

Prior to Rev. Reg. 12-94, the requisites for a refund were: (1) the income tax return for the previous year must show that income payment (rental in this case) was reported as part of the gross income; and (2) the withholding tax statement of the

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withholding tax agent must show that payment of the creditable withholding tax was made. However, even without this regulation, the commissioner may inspect the books of the taxpayer and reassess a taxpayer for deficiency tax payments under Sections 7, NIRC. We stress that what was required under Rev. Reg. 12-94 was only a submission of records but the verification of the tax return remained the function of the commissioner.

Worth emphasizing are these uncontested facts: (1) the amounts withheld were actually remitted to the BIR and (2) the final adjusted returns — which the BIR did not question — showed that, for 1979 and 1980, no income taxes from petitioner were due. Hence, under the principle of *solutio indebiti* provided in Art. 2154, Civil Code,[26] the BIR received something when "there [was] no right to demand it," and thus "the obligation to return arises."[27] Heavily militating against Respondent Commissioner is the ancient principle that no one, not even the state, shall enrich oneself at the expense of another. Indeed, simple justice requires the speedy refund of the wrongly held taxes.

WHEREFORE, the assailed Decision is hereby *REVERSED* and the decision of the Court of Tax Appeals is *REINSTATED.* No costs.

SO ORDERED.

Narvasa, C.J. (Chairman), Romero, Melo, and *Francisco, JJ.*, concur.

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[26] "ART. 2154. If something is received when there is no right to demand it, and it was unduly delivered through mistake, the obligation to return it arises."

[27] *Ramie Textiles, Inc. vs. Mathay, Sr.,* 89 SCRA 586, 591-592, April 30, 1979, per De Castro, *J.*