Supreme Court E-Library

[G.R. No. L-26742. April 30, 1970]

REPUBLIC OF THE PHILIPPINES, plaintiff-appellant, *vs.* ANTONIO HERAS, defendant-appellee.

SYLLABUS

1. TAXATION; PAYMENT OF TAXES; PRIVILEGE TO USE BACKPAY CERTIFICATES LIMITED TO ORIGINAL APPLICANTS OF SUCH CERTIFICATES.— The privilege to use backpay certificates for payment of taxes and other obligations to the government is limited by law only to the original applicants of such certificates and does not extend to the subsequent assignees or holders thereof.

2. ID.; ID.; ID.; CLEAR UNDER SECTION 2 OF R.A. 304; PAYMENT BY ASSIGNEE OF CERTIFICATE, NOT VALID; INSTANT CASE.— That the law indeed confined the privilege of using backpay certificates for payment of taxes to the original applicants thereof is clear from the pertinent provisions of Section 2 of Republic Act 304, as amended by Republic Act 800 and 897. Heras not being the original applicant of the certificates involved, the effected payment of his tax obligation by means of such certificates constituted no valid payment at all. Consequently, his tax liability not only remained unextinguished; he even became subject to surcharges and penalties for late payment of tax.

3. ID.; ID.; ID.; ID.; INTENT OF LAWMAKING BODY.— It may be observed that in enumerating (in the first half of the quoted section) the obligations that may properly be settled with the use of backpay certificates, the law referred to them as "his taxes," government hospital bills of "the applicant," lands purchased or leased "by him," and any amount received by "the applicant," thereby rendering unmistakable the intent of the lawmaking body, which is to limit the use of these certificates in certain specified cases to the applicants or original holders thereof.

4. ID.; ID.; ID.; ID.; SECTION 2 OF R.A. 304, EXPLAINED.— The first part of Section 2 of R.A. 304, allowing its acceptance by the government for the settlement of applicant's obligations, is by certificates of limited negotiability, transferable only by indorsement to the applicant's creditor and no further ("Provided, furthermore, that no certificate shall be transferred by indorsement more than once") and at a discount of not more than 2% per annum; while those

Supreme Court E-Library

certificates negotiable to any citizen, bank or financial institution at least 60% of whose capital is Filipino-owned, at a discount not exceeding 3 1/2% per annum for ten years, are made without the privilege of applying them to the payment of similar obligations of the indorsees or persons to whom they are negotiated.

5. ID.; ID.; CASES OF *TAN vs. VETERANS BACKPAY COMMISSION* (L-12944, 30 March 1969, 105 Phil. 377) and *TIRONA vs. CUDIAMAT* (L-21235, 31 May 1965, 14 SCRA 264), EXPLAINED.— While it is true that we declared in the Tan case that backpay certificates may be utilized for payment of obligations to the Government, such as taxes, government hospital bills, etc., and in the Tirona case, that the applicability of such certificates for payment of taxes is without limitation in point of time, such rulings are understood to be applicable only where the payment of taxes with certificates is proper, i.e., where they are used for settlement of the applicants' tax liabilities.

6. ID.; ID.; LIABILITY FOR SURCHARGE AND INTEREST.— Appellee is liable for surcharges and interests on the unpaid tax under Sec. 51-e(2) and (3) of the Internal Revenue Code which provides that where deficiency tax is not paid in full, there shall be collected upon the unpaid amount, as part of the tax, interest of 1% a month, but not to exceed the amount corresponding to 3 years, plus 5% surcharge, such surcharge and interests to be computed from notice of the assessment or demand therefor by the Commissioner. For once informed of the basis of the demand by the Commissioner-in this case, of the existence of the BIR circular disallowing acceptance of backpay certificates for settlement of the tax obligations of assignees or subsequent holders thereof-the refusal of the taxpayer to pay the demanded tax cannot be considered as made in good faith that would relieve him of liability for payment of surcharges and interests.

7. ID.; ID.; ID.; INTERESTS, COMPENSATORY IN NATURE.— The interest collectible is not punitive in nature, but compensatory; it is a compensation to the State for the delay in the payment of the tax. It is the charge for the use by the taxpayer of funds that rightfully should have been in the government coffers and utilized for the ends thereof (Castro *v.* Collector, L-12174, 28 December 1962, 6 SCRA 886).

8. REMEDIAL LAW; NOTICES; NOTICE SHOULD BE SERVED TO THE PROPER LEGAL DIVISION OR SECTION WHERE LAWYER WORKS IN CASES WHERE GOVERNMENT IS PARTY; CASE AT BAR.— The addressing of copy of the decision

Supreme Court E-Library

to Atty. Jesus Licopit, who has then been transferred to another division of the Internal Revenue Office did not constitute valid service on plaintiff, for in cases where the government is a party, notice should be served to the proper legal division or section of the Bureau or Department concerned and not to the lawyer of the government personally.

APPEARANCES OF COUNSEL

Solicitor General Antonio P. Barredo, Asst. Sol. Gen. Felicisimo R. Rosete, Sol. Lolita O. Galang and *Special Atty. Valentin A. Festejo* for plaintiff-appellant.

Norberto J. Quisumbing for defendant-appellee.

DECISION

REYES, J.B.L., *J.*:

The Republic of the Philippines is here appealing from the decision of the Court of First Instance of Rizal (in Civil Case No. Q-7987) holding as valid the payment of income taxes by means of backpay certificates by assignees or holders thereof, contrary to our ruling in De Borja *vs.* Gella, L-18330, 31 July 1963, 8 SCRA 602.

The records of this case establish the following facts:

On 30 April 1959, Antonio Heras filed his income tax return for 1958 declaring a taxable net income of ₱62,444.64. Upon audit and examination of the return, the Bureau of Internal Revenue found as due and collectible from said taxpayer the sum of ₱13,962.00. The corresponding demand therefor was made under Income Tax Assessment Notice No. 43-1-415-833-58, dated 14 May 1959. On 17 August 1959, the taxpayer paid the tax said to be due to the Municipal Treasurer of Bacoor, Cavite, by means of negotiable certificates of indebtedness in the sum of ₱13,934.55 and cash in the amount of ₱27.45, or a total of ₱13,962.00.

On 12 August 1960 and 3 November 1960, the Revenue office notified the taxpayer that, pursuant to BIR General Circular No. V-289 dated 8 May 1959, payment of income taxes with indorsed negotiable backpay certificates is not allowed, and thus required

Supreme Court E-Library

that the tax supposedly unsettled be paid. And when another demand for payment, made on 7 April 1964, remained unheeded, an action was instituted by the Republic of the Philippines against taxpayer Antonio Heras in the Court of First Instance of Rizal (Quezon City, Civil Case No. Q-7987) for collection of the alleged deficiency income tax in the sum of ₱13,934.55; ₱697.00, as 5% surcharge thereon; plus 1% monthly interest on the amount from 31 May 1959 amounting to ₱5,016.00,[1] or a total of ₱19,637.04.

Traversing the allegations of the complaint, defendant taxpayer set up as affirmative defenses (a) the *validity* of his tax payment to the Municipal Treasurer of Bacoor, Cavite, on 17 August 1959; (b) that having accepted such payment plaintiff Republic of the Philippines was *estopped* from pursuing the complaint; and (c) that the opinion of the Secretary of Justice (Op. No. 69, s. 1959), upon which Circular No. V-289 of the Internal Revenue Office was based, is *not* binding upon the courts.

In its decision of 14 May 1966, the court rendered judgment for the taxpayer and held as valid and effective the payment of the defendant's 1958 income tax by the use of indorsed negotiable backpay certificates.

The issues presented in this case are simple, viz., (1) whether or not negotiable certificates of indebtedness or backpay certificates may be used for payment of their tax liabilities by holders who are *not the original applicants* therefor; and (2) whether or not herein appellee taxpayer is liable for surcharges and interests for late payment of his 1958 income tax.

It is not denied that the negotiable certificates of indebtedness utilized by appellee in paying his 1958 deficiency income tax were not originally issued to him but to the following persons:

NCI No.	*Amount*	*Applicant for Backpay Rights*	*Registered Assignees*
16619	₱ 65.42	Benito B. Reparip	Josefina Peralta
16620	66.14	Servillano Magtoto	Josefina Peralta

[1] For a period of 36 months, in accordance with Section 51-e(2), Internal Revenue Code.

Supreme Court E-Library

16621	135.25	Eulogio Fulgar	Josefina Peralta
16622	66.14	Domingo P. Palay	Josefina Peralta.
16634	1,0/8.12	Enrique Muyal	Simeona Alcantara
16579	80.83	Jose M. Ursabia	Josefina Peralta
16580	12,376.41	Vicenta Lagrosa	Eusebio Lagrosa
19924	66.14	Maximo S. Manabat	Josefina Peralta
Total	P13,935.05		

Assailing the correctness of the judgment of the court below that there had been valid settlement of the appellee's tax liability, appellant Republic of the Philippines contends that the privilege to use backpay certificates for payment of taxes and other obligations to the government is limited by law [2] only to the *original* applicants of such certificates and does not extend to subsequent assignees or holders thereof; that appellee Heras not being the original applicant of the cetificates involved herein, the effected payment of his tax obligation by means of such certificates constituted no valid payment at all. Consequently, according to appellant, Heras' tax liability not only remained unextinguished; he even became subject to surcharges and penalties for late payment of tax.

This contention of appellant is not unmeritorious; it is supported by the ruling in the case of *De Borja vs. Gella, supra,* wherein this Court, passing upon the same issue of whether or not the subsequent holder or assignee of a certificate of indebtedness could use backpay certificates for the settlement of tax obligations, declared:

"----------. Neither can it be contended that appellee can compel the government to accept the alleged certificates of indebtedness in payment of his real estate taxes under proviso No. 2 above-quoted (of Rep. Act 304, as amended) also for the reason that in order that such payment may be allowed the tax must be owed by the *applicant himself.* This is the correct implication that may be drawn from the use by the law of the words *'his taxes.'* Verily, the right to use the backpay certificate in settlement of taxes is given only to the applicant and not to any holder of any negotiable certificate to whom the law only gives the right to have it discounted by

[2] Section 2, Republic Act 304, as amended by Republic Acts 800 and 897.

Supreme Court E-Library

a Filipino citizen or corporation under certain limitations. Here appellee is not himself the applicant of the certificate in question. He is merely an assignee thereof, or a subsequent holder whose right is at most to have it discounted upon maturity -- or to negotiate it in the meantime. ------."

That the law indeed confined the privilege of using backpay certificates for payment of taxes to the original applicants thereof is clear from the pertinent provisions of Section 2 of Republic Act 304, as amended by Republic Act 800 and 897, thus:

"SEC. 2. The Treasurer of the Philippines shall, upon application of all persons specified in Section one hereof and within one year from the approval of this amendatory Act, and under such rules and regulations as may be promulgated by the Secretary of Finance, acknowledge and file requests for the recognition of the right to the salaries or wages as provided in Section one hereof, and notice of such acknowledgment shall be issued to the applicant which shall state the total amount of such salaries or wages due the applicant, and certify that it shall be redeemed by the Government of the Philippines within ten years from the date of their issuance without interest: *Provided,* That upon application and subject to such rules and regulations as may be approved by the Secretary of Finance a certificate of indebtedness may be issued by the Treasurer of the Philippines covering the whole or a part of the total salaries or wages the right to which has been duly acknowledged and recognized, provided that the face value of such certificate of indebtedness shall not exceed the amount that *the applicant may need for the payment of* (1) obligations subsisting at the time of the approval of this amendatory Act for which the applicant may directly be liable to the Government or to any of its branches or instrumentalities, or the corporations owned or controlled by the Government, or to any citizen of the Philippines, or to any association or corporation organized under the laws of the Philippines, who may be willing to accept the same for such settlement; (2) *his taxes;* (3) government hospital bills *of the applicant;* (4) lands purchased or leased or to be purchased or leased *by him* from the public domain; and (5) any amount received *by the applicant* as gratuity or pension which he has to refund to the Government or to any of its branches or instrumentalities: "*Provided, further,* That such settlement shall be effected by indorsement on the instrument: *Provided, furthermore,* That no certificate shall be transferred or ceded by indorsement more than once, nor at a discount rate exceeding two *per centum per annum: And provided, also,* That any person who is not an alien, bank or other financial institution at least sixty *per centum* of whose capital is owned by Filipinos may, notwithstanding any provision of its charter, articles of incorporation, by-

Supreme Court E-Library

laws, or rules and regulations to the contrary, accept or discount at not more than three and one-half *per centum per annum* for ten years a negotiable certificate of indebtedness which shall be issued by the Treasurer of the Philippines upon application by a holder of back pay acknowledgment: --------." (Italics supplied)

It may be observed that in enumerating (in the first half of the quoted section) the obligations that may properly be settled with the use of backpay certificates, the law referred to them as "his taxes," government hospital bills of "the applicant," lands purchased or leased "by him," and any amount received by "the applicant," thereby rendering unmistakable the intent of the law-making body, which is to limit the use of these certificates in certain specified cases to the applicants or original holders thereof.

Appellee, however, claims that to sustain appellant's stand would be to circumscribe the negotiability of the certificate prescribed in the later part of the section (after the words *and provided also*) and thus defeat the purpose of the law. This is not correct. The first part of the section quoted earlier, allowing its acceptance by the government for the settlement of applicant's obligations, is by certificates of limited negotiability, transferable only by indorsement to the applicant's creditor and no further ("Provided, furthermore, that no certificate shall be transferred by indorsement more than once") and at a discount of not more than 2% per annum; while those certificates negotiable to any citizen, bank or financial institution at least 60% of whose capital is Filipino-owned, at a discount not exceeding 3 1/2% per annum for ten years, are made without the privilege of applying them to the payment of similar obligations of the indorsees or persons to whom they are negotiated.

Neither would it be correct to conclude that there has been valid payment of appellee's tax in this case on the basis of our rulings in the cases of *Tan vs. Veterans Backpay Commission*[3] and *Tirona vs. Cudiamat*.[4] For while it is true that we declared

[3] L-12944, 30 March 1959, 105 Phil. 377.

[4] L-21235, 31 May 1965, 14 SCRA 264.

Supreme Court E-Library

in the *Tan* case that backpay certificates may be utilized for payment of obligations to the Government, such as taxes, government hospital bills, etc., and, in the *Tirona* case, that the applicability of such certificates for payment of taxes is without limitation in point of time, such rulings are understood to be applicable only where the payment of taxes with certificates is proper, i.e., where they are used for settlement of the applicants' tax liabilities.

The question now is should appellee be held liable also for surcharges and interests on the unpaid tax? The answer is in the affirmative. Under Section 51-e (2) and (3) of the Internal Revenue Code, where deficiency tax is not paid in full, there shall be collected upon the unpaid amount, as part of the tax, interest of 1% a month, but not to exceed the amount corresponding to 3 years, plus 5% surcharge, such surcharge and interests to be computed from notice of the assessment or demand therefor by the Commissioner.[5] For once, informed of the basis of the demand by the Commissioner - in this case, of the existence of the BIR circular disallowing acceptance of backpay certificates for settlement of the tax obligations of assignees or subsequent holders thereof - the refusal of the taxpayer to pay the demanded tax cannot be considered as made in good faith that would relieve him of liability for payment of surcharges and interests.[6] It may even be mentioned that, in the present case, appellee's act of tendering payment, with backpay certificates, of the deficiency tax is an acknowledgment that the said tax is really due and demandable. There having been, as we hereby affirm, an invalid payment of appellee's tax liability, which constituted no payment at all, the collection of surcharges and interests thereon from said taxpayer becomes mandatory on the Commissioner of Internal Revenue and the courts.[7] It may not be amiss to state further

[5] Republic *vs.* Razon, L-17462 & L-17472, 29 May 1967, 20 SCRA 234; Central Azucarera Don Pedro *vs.* CTA, L-23236 & L-23254, 31 May 1967, 20 SCRA 344; Republic *vs.* Lim Tian Teng Sons & Co., Inc., L-21731, 31 March 1966, 16 SCRA 584.

[6] Connel Bros. *vs.* Collector, L-15470, 31 March 1964, 10 SCRA 469.

[7] Pirovano *vs.* Commissioner, L-19865, 31 July 1965, 14 SCRA 832.

Supreme Court E-Library

that the interests collectible here is not punitive in nature, as appellee would like to impress, but compensatory; it is compensation to the state for the delay in the payment of the tax. It is the charge for the use by the taxpayer of funds that rightfully should have been in the government coffers and utilized for the ends thereof.[8]

As regard appellee's allegation that the present appeal was filed out of time and, therefore, should be dismissed, we find it to be without merit. It appears from the records that the complaint in the court below was filed for the plaintiff by BIR Special Counsel Jesus Licopit; that said counsel was later transferred to another division of the Internal Revenue Office and the case was assigned to Atty. Valentin Festejo, also of the same office, who entered appearance therein and actually attended the court hearings. When the decision was rendered, however, copy thereof was sent by registered mail to Atty. Licopit, and it was returned to the court unclaimed. On 6 May 1966, learning of the rendition of the decision, Atty. Festejo moved for the service of the decision on him. The motion was granted, and said lawyer was furnished copy of the decision on 14 May 1966. On 24 May 1966, he filed a motion for reconsideration, which was denied on 15 August 1966. Copy of this order of denial was received by said counsel on 22 August 1966. On 12 September 1966, the record on appeal was filed and approved by the trial court.

It can be seen from the foregoing narration of facts that service of the decision was considered made upon the plaintiff only on 14 May 1966, thus making timely the filing of the record on appeal on 12 September 1966. And this is not incorrect; the addressing of copy of the decision to Jesus T. Licopit, Special Attorney, c/o Bureau of Internal Revenue, Cubao, Quezon City,[9] did not constitute valid service on said plaintiff. We have here not an instance of two counsels of record appearing for a party, where

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[8] Castro *vs.* Collector, L-12174, 28 December 1962, 6 SCRA 886.

[9] Since July 1964, Atty. Licopit was already working in the Internal Security Division, Bureau of Internal Revenue, in the Department of Finance building in Manila.

Supreme Court E-Library

the service of notice to one is considered valid and complete service upon the party. The counsel for the plaintiff was only the proper legal division or section of the Bureau of Internal Revenue, not Atty. Licopit or Atty. Festejo personally. Considering that the records would have shown that Atty. Festejo was already appearing in the case, notice of the decision at least should have been sent to him.

WHEREFORE, the decision of the lower court appealed from is hereby set aside, and appellee Antonio Heras is ordered to pay to appellant Republic of the Philippines the sum of ₱13,934.55 as deficiency income tax; 1% monthly interest on the said unpaid tax, but not to exceed 36%, plus 5% surcharge thereon, computed from notice of the assessment thereof by the Commissioner of Internal Revenue, until the total amount due is fully paid. No costs.

Concepcion, C.J., Dizon, Makalintal, Zaldivar, Ruiz Castro, Teehankee and *Villamor, JJ.*, concur.

Fernando, J., did not take part.

Barredo, J., is on leave.

Decision set aside.

[G.R. No. L-27454. April 30, 1970]

ROSENDO O. CHAVES, plaintiff-appellant, *vs.* FRUCTUOSO GONZALES, defendant-appellee.

SYLLABUS

1. CIVIL LAW; CONTRACTS; BREACH OF CONTRACT FOR NON-PERFORMANCE; FIXING OF PERIOD BEFORE FILING OF COMPLAINT FOR NON-PERFORMANCE, ACADEMIC.— Where the time for compliance had expired and there was breach of contract by non-performance, it was academic for the plaintiff to have first petitioned the court to fix a period for the performance of the contract before filing his complaint.

2. ID.; ID.; ID.; DEFENDANT CANNOT INVOKE ARTICLE 1197 OF THE CIVIL CODE OF THE PHILIPPINES.— Where the defendant