

**REPUBLIC OF THE PHILIPPINES, PLAINTIFF AND APPELLANT, VS.
PAZ ARGUELLES VDA. DE LAO, CARMEN LAO, PACITA TERESA LAO
AND CONCEPCION LAO, DEFENDANTS AND APPELLEES.**

G.R. No. L-16513. January 31, 1962

Ponente: LABRADOR, J.

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LABRADOR, J.:

Appeal from a judgment of the Court of First Instance of Manila, Hon. Carmelino G. Alvendia, presiding, the dispositive portion of which reads as follows:

"* * * The alternative cause of action contained in defendants' answer is well taken. The sum of P2,198 representing the income tax due from the estate of Gabriel Lao for the year 1950 should be deducted from the estate, subject to the estate tax and since said estate tax without this deduction has already been paid, the Collector of Internal Revenue should recompute the estate tax and the overpayment should be deducted from the deficiency income tax now being claimed against the heirs of Gabriel Lao."

"* * * WHEREFORE, the Court orders the defendants jointly and severally to pay the plaintiff the difference between P2,198 representing deficiency income tax due from the estate of the deceased Gabriel Lao and the sum of the tax credit to which the estate of Gabriel Lao is entitled as a result of the reduction of the estate subject to inheritance due to the deficiency income tax of P2,198 and the tax credits due to each of defendants for the over payment in inheritance taxes made by each of them." (ROA, pp. 36-37.)

On January 8, 1958, the Republic of the Philippines filed the present action in the Court of First Instance of Manila for the recovery of the amount of P2,198.00 as deficiency income tax of the spouses Gabriel Lao, now deceased, and Paz Arguelles de Lao, for the year 1950, plus surcharge of 5% and interests thereon. The complaint alleged that on April 16, 1961, the spouses filed a joint income tax return for the year 1950, showing a net income of P36,889.91; that on the basis of said return, a revised assessment notice was issued by the Bureau of Internal Revenue on July 6, 1953, imposing an additional tax of P2,840.00 on both spouses for said taxable income; that on August 5, 1953, after Gabriel Lao had died, the lawyer of the spouses requested the Collector of Internal Revenue for reinvestigation, and pursuant thereto another assessment was made on August 3, 1954, reducing the sum to P2,198.00; that on August 3, 1954, the Collector demanded payment of the said amount of income tax for 1950 on or before September 15, 1954; that upon failure of the heirs of the late Gabriel Lao and his wife to pay said amount, the Collector imposed a surcharge of 5% on the sum of P2,198.00 and an interest thereon at the rate of 1% per month from September 16, 1954 until fully paid and P20.00 as compromise penalty for late payment; that neither the amount due nor the surcharge and interest were paid.

The defendants filed their answer on February 5, 1958, admitting the making of the assessment against the spouses and the giving of notice thereof to the latter or their representatives, and their refusal to pay the tax for the year 1950, in the amount of P2,198.00. They claim, as a defense, that they had actually made payment thereof, or that if no payment had been made, the collection of the tax has prescribed because more than two years have elapsed since the same should have been collected, and that notwithstanding the Collector's knowledge of the

death of said Gabriel Lao he failed and neglected to demand said taxes within said period of time. In a paragraph captioned "Alternative Cause of Action", the defendants allege:

"14. Assuming arguendo that the sum of P2,198.00 as claimed by the plaintiff as supposed income tax of the late Don Gabriel Lao for 1950 is proper, yet the same is a proper deduction from the estate of the said deceased, and said amount will naturally proportionately reduce the estate and inheritance taxes payable by the defendant's." (par. 14, p. 29 ROA).

After trial, the trial court found the following facts: On April 16, 1951, a joint income tax return of the spouses Gabriel Lao and Paz Arguelles was filed with the Bureau of Internal Revenue. At first, an assessment of P9,100 was imposed and this was paid by the spouses. Subsequently, however, an additional deficiency income tax of P2,480.00 was imposed, for which an assessment notice was sent on July 6, 1953. When said assessment was sent, Gabriel Lao was already dead, but the notice was received by his widow. The deficiency income tax was reduced to P2,198.00 after a reinvestigation of the assessment upon the request of the lawyers of the spouses in a letter dated August 5, 1953.

The trial court found that the estate of the deceased Gabriel Lao and his wife are liable for the sum of P2,198.00. However, it ordered the plaintiff to recompute the estate tax of said Gabriel Lao and ordered defendants to pay the plaintiff the difference between the deficiency tax of P2,198.00 and the amount of the tax credit to which the estate is entitled, as a result of the recomputation of the estate tax. Consequently, the Republic has appealed to this Court.

Before this Court, the appellant argues that the decision of the court below allowing recomputation and credit for overpayment of taxes already paid violates the provisions of Sections 306 and 309 of the National Internal Revenue Code, which read as follows:

"SEC. 306.—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 wrongful collected, until a claim for refund or credit has been duly filed with the Collector of Internal Revenue; x x x 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."

* * * * *

"SEC. 309.—The Collector of Internal Revenue may compromise any civil or other case arising under this Code or other law or part of law administered by the Bureau of Internal Revenue, may credit or refund taxes erroneously or illegally received, or penalties imposed without authority, and may remit before payment any tax that appears to be unjustly assessed or excessive."

"* * * The authority of the Collector of Internal Revenue to credit or refund taxes or penalties under this section can only be exercised if the claim for credit or refund is made in writing and filed with him within two years after the payment of the tax or penalty."

While section 309 permits the Collector of Internal Revenue to compromise any action or claim arising under the National Internal Revenue Code, and credit taxes erroneously or illegally received, this power is subject to the provision of section 306 to the effect that before a proceeding can be maintained for the recovery of an internal revenue tax erroneously or illegally assessed or collected, a claim for refund or credit of the tax claimed to have been erroneously or illegally collected must be filed with the Collector of Internal Revenue within two years from the date of the payment of the tax or the penalty. The presentation of the claim for refund within the two-year period is a mandatory provision which is a condition precedent to the approval of a taxpayer's right of action for

refund. (See *Johnston Lumber Co., Inc. vs. Court of Tax Appeals, et al.*, 101 Phil., 151; 50 Off. Gaz., 5226, and cases cited therein.) The claim for refund is stated in the defendant's "alternative cause of action," wherein it is claimed that the amount of P2,198.00 assessed as deficiency income tax should first be deducted from the estate of Don Gabriel Lao, and the reduction in the estate tax caused by the reduction of the estate in the amount of P2,198, be credited in favor of the estate against the deficiency income tax herein sought to be recovered. The deficiency income tax was assessed on August 3, 1954 and payment thereof was demanded by the Collector of Internal Revenue on or before September 15, 1954. But the defendants' answer in the case at bar, which contains the "alternative cause of action" was presented on February 25, 1958, or a period of three years and five months after the demand for the payment of the tax was made. Consequently, the demand for the credit of the supposed overpaid tax against the deficiency income tax of P2,198, clearly falls within the prohibition contained in section 306 of the National Internal Revenue Code above quoted.

Wherefore, the judgment appealed from is hereby reversed and the defendants ordered to pay the amount demanded in the complaint, P2,198, plus 5% surcharge and 1% monthly interest thereon beginning September 16, 1954 to the date of full payment, and P20 as compromise penalty for late payment. Without costs. So ordered.

Bengzon, C. J., Padilla, Bautista Angelo, Concepcion, Reyes, J. B. L., Barrera, Paredes, Dizon, and De Leon, JJ., concur.

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