

SECOND DIVISION

[G.R. No. 164050, July 20, 2011]

MERCURY DRUG CORPORATION, PETITIONER, VS. COMMISSIONER OF INTERNAL REVENUE, RESPONDENT.

D E C I S I O N

PEREZ, J.:

This petition for review on *certiorari* calls for an interpretation of the term "cost" as used in Section 4(a) of Republic Act No. 7432, otherwise known as "*An Act to Maximize the Contribution of Senior Citizens to Nation Building, Grant Benefits and Special Privileges and For Other Purposes.*"

A rundown of the pertinent facts is presented below.

Pursuant to Republic Act No. 7432, petitioner Mercury Drug Corporation (petitioner), a retailer of pharmaceutical products, granted a 20% sales discount to qualified senior citizens on their purchases of medicines. For the taxable year April to December 1993 and January to December 1994, the amounts representing the 20% sales discount totalled P3,719,287.68^[1] and P35,500,593.44,^[2] respectively, which petitioner claimed as deductions from its gross income.

Realizing that Republic Act No. 7432 allows a tax credit for sales discounts granted to senior citizens, petitioner filed with the Commissioner of Internal Revenue (CIR) claims for refund in the amount of P2,417,536.00 for the year 1993 and P23,075,386.00 for the year 1994. Petitioner presented a computation^[3] of its overpayment of income tax, thus:

TAXABLE YEAR 1993

SALES, Net	P10,228,518,335.00
Add: Cost of 20% Discount to Senior Citizens	3,719,288.00
SALES, Gross	P10,232,237,623.00

COST OF SALES

Merchandise Inventory, Beg.	P2,427,972,150.00	
Purchases	8,717,393,710.00	
Goods Available for Sales	P11,145,365,860.00	
Merchandise	2,458,743,127.00	8,686,622,733.00

Inventory, End		
GROSS PROFIT		P1,545,614,890.00
Add: Miscellaneous Income		<u>58,247,973.00</u>
TOTAL INCOME		P1,603,862,863.00
OPERATING EXPENSES		<u>1,226,816,343.00</u>
NET INCOME BEFORE TAX		P 377,046,520.00
Less: Income subjected to final income tax		<u>20,966,602.00</u>
NET TAXABLE INCOME		<u>P 356,079,918.00</u>
INCOME TAX PAYABLE		P 124,627,972.00
LESS: TAX CREDIT (20% Sales Discount to Senior Citizens)	P 3,719,288.00	
TAX ACTUALLY PAID	<u>123,326,220.00</u>	<u>127,045,508.00</u>
TAX REFUNDABLE		<u>P 2,417,536.00</u>

x x x x

TAXABLE YEAR 1994

SALES, Net	P 11,671,366,402.00
Add: Cost of 20% Sales Discount to Senior Citizens	<u>35,500,594.00</u>
SALES, Gross	P11,706,866,996.00
COST OF SALES	
Merchandise Inventory, Beg.	P2,458,743,127.00
Purchases	<u>10,316,941,308.00</u>
Goods Available for Sales	P12,775,684,435.00

Less: Merchandise	<u>2,928,397,228.00</u>		<u>9,847,287,207.00</u>
Inventory, End			
GROSS PROFIT			P1,859,579,789.00
Add: Miscellaneous			<u>68,809,864.00</u>
Income			
TOTAL INCOME			P1,928,389,653.00
OPERATING			<u>1,499,422,645.00</u>
EXPENSES			
NET INCOME BEFORE			428,967,008.00
TAX			
Less: Income			<u>25,591,586.00</u>
subjected to final			
Income tax			
NET TAXABLE INCOME			<u>P 403,375,422.00</u>
INCOME TAX PAYABLE			P 141,181,398.00
LESS: TAX CREDIT			
(Cost of 20%			
Discount to		P 35,500,594.00	
Senior			
Citizens)			
TAX		<u>128,756,190.00</u>	<u>164,256,784.00</u>
ACTUALLY			
PAID			
TAX REFUNDABLE		<u>P 23,075,386.00</u>	

When the CIR failed to act upon petitioner's claims, the latter filed a petition for review with the Court of Tax Appeals. On 6 September 2000, the Court of Tax Appeals rendered the following judgment:^[4]

WHEREFORE, in view of the foregoing, the instant Petition for Review is hereby PARTIALLY GRANTED. Accordingly, Revenue Regulations No. 2-94 of the Respondent is declared null and void insofar as it treats the 20% discount given by private establishments as a deduction from gross sales. Respondent is hereby ORDERED to GRANT A REFUND OR ISSUE A TAX CREDIT CERTIFICATE to Petitioner in the reduced amount of P1,688,178.43 representing the latter's overpaid income tax for the taxable year 1993. However, the claim for refund for taxable year 1994 is denied for lack of merit.^[5]

The Court of Tax Appeals favored petitioner by declaring that the 20% sales discount should be treated as tax credit rather than a mere deduction from gross income. The Court of Tax Appeals however found some discrepancies and irregularities in the cash slips submitted by petitioner as basis for the tax refund. Hence, it disallowed the claim for taxable year 1994 and some portion of the amount claimed for 1993 by petitioner, viz:

So, contrary to the allegation of Petitioner that it granted 20% sales discounts to senior citizens in the total amount of P3,719,888.00 for taxable year 1993 and P35,500,554.00 for taxable year 1994, this Court's study and evaluation of the evidence show that for taxable year 1993 only the amounts of P3,522,123.25 and for 1994, the amount of P8,789,792.27 were properly substantiated. The amount of P3,522,123.25 corresponding to 1993 will be further reduced to P2,989,930.43 as this Court's computation is based on the cost of the 20% discount and not on the total amount of the 20% discount based on the decision of the Court of Appeals in Commissioner of Internal Revenue v. Elmas Drug Corporation, CA-SP No. 49946 promulgated on October 19, 1999, where it ruled:

"Thus the cost of the 20% discount represents the actual amount spent by drug corporations in complying with the mandate of RA 7432. Working on this premise, it could not have been the intention of the lawmakers to grant these companies the full amount of the 20% discount as this could be extending to them more than what they actually sacrificed when they gave the 20% discount to senior citizens." (Underscoring supplied).

Similarly the amount of P8,789,792.27 corresponding to taxable year 1994 will be reduced to P7,393,094.28 based on the aforementioned Court of Appeals decision. These reductions are illustrated as follows:

TAXABLE YEAR 1993

Cost of Sales		P
	8,686,622,733.00	
Divided by Gross Sales	<u>10,232,237,623.00</u>	
Cost of Sales Percentage	<u>84.89%</u>	
Adjusted Amount of 20% Discount given to Senior Citizens	3,522,123.25	
Multiply by	<u>84.89%</u>	
Allowable Tax Credit	<u>P 2,989,930.43</u>	

TAXABLE YEAR 1994

Cost of Sales	P9,847,287,207.00
Divided by Gross Sales	<u>11,706,866,996.00</u>
Cost of Sales Percentage	<u>84.11%</u>
Adjusted Amount of 20% Discount given to Senior Citizens	P 8,789,792.27
Multiply by	<u>84.11%</u>
Allowable Tax Credit	P 7,393,094.28

With the foregoing changes in the amount of discounts granted by Petitioner in 1993 and 1994, it necessarily follows that adjustments have to be made in the computation of the refundable amount which is entirely different from the computation presented by the Petitioner. This Court's conclusion is that Petitioner is only entitled to a tax credit of P1,688,178.43 for taxable year 1993 detailed as follows:

**TAXABLE
YEAR 1993**

Sales, Net	P10,228,518,335.00	
Add: Cost of 20% Discount given to Senior Citizens	<u>3,719,288.00</u>	
SALES, Gross	P10,232,237,623.00	
COST OF SALES		
Merchandise Inventory, Beg.	P2,427,972,150.00	
Add: Purchases	<u>8,717,393,710.00</u>	
Total goods available for sale	P1,145,365,860.00	
Less:	<u>2,458,743,127.00</u>	<u>8,686,622,733.00</u>
Merchandise Inventory, End		
GROSS PROFIT	P 1,545,614,890.00	
Add:	<u>58,247,973.00</u>	
Miscellaneous Income		
TOTAL INCOME	P 1,603,862,863.00	
OPERATING EXPENSES	<u>1,226,816,343.00</u>	
NET INCOME BEFORE TAX	P 377,046,520.00	
Less: Income subjected to final income tax	<u>20,966,602.00</u>	
NET TAXABLE INCOME	P 356,079,918.00	
INCOME TAX PAYABLE	P 124,627,972.00	
LESS: TAX CREDIT (20% Sales Discount given to Senior Citizens)	P 2,989,930.43	
TAX ACTUALLY PAID	<u>123,326,220.00</u>	<u>126,316,150.43</u>
TAX	P <u>1,688,178.43</u>	