535 Phil. 481

# FIRST DIVISION

# [ G.R. NO. 159593, October 16, 2006 ]

## COMMISSIONER OF INTERNAL REVENUE, PETITIONER, VS. MIRANT[1] PAGBILAO CORPORATION (FORMERLY SOUTHERN ENERGY QUEZON, INC.), RESPONDENT.

## D E C I S I O N

**CHICO-NAZARIO, J.:**

Before this Court is a Petition for Review[2] under Rule 45 of the 1997 Rules of Civil Procedure assailing the Decision,[3] dated 30 July 2003, of the Court of Appeals in CA-G.R. SP No. 60783, which affirmed *in toto* the Decision,[4] dated 11 July 2000, of the Court of Tax Appeals (CTA) in CTA Case No. 5658. The CTA partially granted the claim of herein respondent Mirant Pagbilao Corporation (MPC) for the refund of the input Value Added Tax (VAT) on its purchase of capital goods and services for the period 1 April 1996 to 31 December 1996, and ordered herein petitioner Commissioner of the Bureau of Internal Revenue (BIR) to issue a tax credit certificate in the amount of P28,744,626.95.

There is no dispute as to the following facts that gave rise to the claim for refund of MPC, as found by the CTA[5] -

> [MPC] is a domestic corporation duly organized and existing under and by virtue of the laws of the Philippines with principal office address in Pagbilao Grande Island, Pagbilao, Quezon. It is licensed by the Securities and Exchange Commission to principally engage in the business of power generation and subsequent sale thereof (Exh. A). It is registered with the Bureau of Internal Revenue as a VAT registered entity with Certificate of Registration bearing RDO Control No. 96-600-002498, dated January 26, 1996.
>
> For the period April 1, 1996 to December 31, 1996, [MPC] seasonably filed its Quarterly VAT Returns reflecting an (sic) accumulated input taxes in the amount of P39,330,500.85 (Exhs. B, C, and D). These input taxes were allegedly paid by [MPC] to the suppliers of capital goods and services for the construction and development of the power generating plant and other related facilities in Pagbilao, Quezon (TSN, November 16, 1998, p. 11).
>
> Pursuant to the procedures prescribed under Revenue Regulations No. 7-95, as amended, [MPC] filed on June 30, 1998, an application for tax credit or refund of the aforementioned unutilized VAT paid on capital goods (Exhibit "E").
>
> Without waiting for an answer from the [BIR Commissioner], [MPC] filed

the instant petition for review on July 10, 1998, in order to toll the running of the two-year prescriptive period for claiming a refund under the law.

In answer to the Petition, [the BIR Commissioner] advanced as special and affirmative defenses that "[MPC]'s claim for refund is still pending investigation and consideration before the office of [the BIR Commissioner] accordingly, the filing of the present petition is premature; well-settled is the doctrine that provisions in tax refund and credit are construed strictly against the taxpayer as they are in the nature of a tax exemption; in an action for refund or tax credit, the taxpayer has the burden to show that the taxes paid were erroneously or illegally paid and failure to sustain the said burden is fatal to the action for refund; it is incumbent upon [MPC] to show that the claim for tax credit has been filed within the prescriptive period under the Tax Code; and the taxes allegedly paid by [MPC] are presumed to have been collected and received in accordance with law and revenue regulations.["]

On July 14, 1998, while the case was pending trial, Revenue Officer, Rosemarie M. Vitto, was assigned by Revenue District Officer, Ma. Nimfa Penalosa-Asensi, of Revenue District No. 60 to investigate [MPC]'s application for tax credit or refund of input taxes (Exhs. 1 and 1-a). As a result, a memorandum report, dated August 27, 1998, was submitted recommending a favorable action but in a reduced amount of P49,616.40 representing unapplied input taxes on capital goods. (Exhs. 2, 2-a, 3, and 3-a).

[MPC], due to the voluminous nature of evidence to be presented, availed of the services of an independent Certified Public Accountant pursuant to CTA Circular No. 1-95, as amended. As a consequence, Mr. Ruben R. Rubio, Partner of SGV & Company, was commissioned to verify the accuracy of [MPC]'s summary of input taxes (TSN, October 15, 1998, pp. 3-5). A report, dated March 8, 1999, was presented stating the audit procedures performed and the finding that out of the total claimed input taxes of P39,330,500.85, only the sum of P28,745,502.40 was properly supported by valid invoices and/or official receipts (Exh. G; see also TSN, March 3, 1999, p. 12).

The CTA ruled in favor of MPC, and declared that MPC had overwhelmingly proved, through the VAT invoices and official receipts it had presented, that its purchases of goods and services were necessary in the construction of power plant facilities which it used in its business of power generation and sale. The tax court, however, reduced the amount of refund to which MPC was entitled, in accordance with the following computation -

| | | |
|---|---|---|
| Total amount of the claim for refund | | P39,330,500.85 |
| Less: Disallowances | | |
| a. Per independent auditor | P10,584,998.45 | |

| | | |
|---|---|---|
| b. Per CTA's examination | 875.45 | 10,585,873.90 |
| | ---------- | ---------- |
| | - | |
| | | P28,744,626.95[6] |
| | | ========== |

Thus, the dispositive portion of the CTA Decision,[7] dated 11 July 2000, reads -

> **WHEREFORE**, in view of the foregoing, [MPC]'s claim for refund is hereby partially **GRANTED**. [The BIR Commissioner] is **ORDERED** to **ISSUE** A TAX CREDIT CERTIFICATE in the amount of P28,744,626.95 representing input taxes paid on capital goods for the period April 1, 1996 to December 31, 1996.

The CTA subsequently denied the BIR Commissioner's Motion for Reconsideration in a Resolution,[8] dated 31 August 2001.

Aggrieved, the BIR Commissioner filed with the Court of Appeals a Petition for Review[9] of the foregoing Decision, dated 11 July 2000, and Resolution, dated 31 August 2001, of the CTA. Notably, the BIR Commissioner identified and discussed as grounds[10] for its Petition arguments that were totally new and were never raised before the CTA, to wit -

1. RESPONDENT BEING AN ELECTRIC UTILITY, IT IS SUBJECT TO FRANCHISE TAX UNDER THEN SECTION 117 (NOW SECTION 119) OF THE TAX CODE AND NOT TO VALUE ADDED TAX (VAT).

2. SINCE RESPONDENT IS EXEMPT FROM VAT, IT IS NOT ENTITLED TO THE REFUND OF INPUT VAT PURSUANT TO SECTION 4.103-1 OF REVENUE REGULATIONS NO. 7-95.

The Court of Appeals found no merit in the BIR Commissioner's Petition, and in its Decision, dated 30 July 2003, it pronounced that: (1) The BIR Commissioner cannot validly change his theory of the case on appeal; (2) The MPC is not a public utility within the contemplation of law; (3) The sale by MPC of its generated power to the National Power Corporation (NAPOCOR) is subject to VAT at zero percent rate; and (4) The MPC, as a VAT-registered taxpayer, may apply for tax credit. Accordingly, the decretal portion of the said Decision[11] reads as follows -

> **WHEREFORE**, premises considered, the *Petition* is **DISMISSED** for lack of merit and the assailed 11 July 2000 *Decision* of respondent Court in CTA Case No. 5658 is hereby **AFFIRMED** *in toto*. No costs.

Refusing to give up his cause, the BIR Commissioner filed the present Petition before this Court on the ground that the Court of Appeals committed reversible error in affirming the Decision of the CTA holding respondent entitled to the refund of the amount of P28,744,626.95, allegedly representing input VAT on capital goods and services for the period 1 April 1996 to 31 December 1996. He argues that (1) The observance of procedural rules may be relaxed considering that technicalities are not ends in themselves but exist to protect and promote the substantive rights of the parties; and (2) A tax refund is in the nature of a tax exemption which must be construed strictly against the taxpayer. He reiterates his position before the Court

of Appeals that MPC, as a public utility, is exempt from VAT, subject instead to franchise tax and, thus, not entitled to a refund of input VAT on its purchase of capital goods and services.

This Court finds no merit in the Petition at bar.

I

***The general rule is that a party cannot change his theory of the case on appeal.***

To recall, the BIR Commissioner raised in its Answer[12] before the CTA the following special and affirmative defenses -

> 3. [MPC]'s claim for refund is still pending investigation and consideration before the office of [the BIR Commissioner]. Accordingly, the present petition is premature;
>
> 4. Well-settled is the doctrine that provisions in tax refund and credit are construed strictly against the taxpayer as they are in the nature of a tax exemption;
>
> 5. In an action for refund or tax credit, the taxpayer has the burden to show that the taxes paid were erroneously or illegally paid and failure to sustain the said burden is fatal to the action for refund;
>
> 6. It is incumbent upon [MPC] to show that the claim for tax credit has been filed within the prescriptive period under the tax code;
>
> 7. The taxes allegedly paid by [MPC] are presumed to have been collected and received in accordance with law and revenue regulations.

These appear to be general and standard arguments used by the BIR to oppose any claim by a taxpayer for refund. The Answer did not posit any allegation or contention that would defeat the particular claim for refund of MPC. Trial proper ensued before the CTA, during which the MPC presented evidence of its entitlement to the refund and in negation of the afore-cited defenses of the BIR Commissioner. It was only after the CTA promulgated its Decision on 11 July 2000, which was favorable to MPC and adverse to the BIR Commissioner, that the latter filed his Petition for Review before the Court of Appeals on 4 October 2000, averring, ***for the very first time***, that MPC was a public utility, subject to franchise tax and not VAT; and since it was not paying VAT, it could not claim the refund of input VAT on its purchase of capital goods and services.

There is a palpable shift in the BIR Commissioner's defense against the claim for refund of MPC and an evident change of theory. Before the CTA, the BIR Commissioner admitted that the MPC is a VAT-registered taxpayer, but charged it with the burden of proving its entitlement to refund. However, before the Court of Appeals, the BIR Commissioner, in effect denied that the MPC is subject to VAT, making an affirmative allegation that it is a public utility liable, instead, for franchise

tax. Irrefragably, the BIR Commissioner raised for the first time on appeal questions of both fact and law not taken up before the tax court, an actuality which the BIR Commissioner himself does not deny, but he argues that he should be allowed to do so as an exception to the technical rules of procedure and in the interest of substantial justice.

It is already well-settled in this jurisdiction that a party may not change his theory of the case on appeal.[13] Such a rule has been expressly adopted in Rule 44, Section 15 of the 1997 Rules of Civil Procedure, which provides -

> SEC. 15. *Questions that may be raised on appeal.* - Whether or not the appellant has filed a motion for new trial in the court below, he may include in his assignment of errors any question of law or fact that has been raised in the court below and which is within the issues framed by the parties.

Thus, in *Carantes v. Court of Appeals*,[14] this Court emphasized that -

> The settled rule is that defenses not pleaded in the answer may not be raised for the first time on appeal. A party cannot, on appeal, change fundamentally the nature of the issue in the case. When a party deliberately adopts a certain theory and the case is decided upon that theory in the court below, he will not be permitted to change the same on appeal, because to permit him to do so would be unfair to the adverse party.

In the more recent case of *Mon v. Court of Appeals*,[15] this Court again pronounced that, in this jurisdiction, the settled rule is that a party cannot change his theory of the case or his cause of action on appeal. It affirms that "courts of justice have no jurisdiction or power to decide a question not in issue." Thus, a judgment that goes beyond the issues and purports to adjudicate something on which the court did not hear the parties, is not only irregular but also extrajudicial and invalid. The rule rests on the fundamental tenets of fair play.

The BIR Commissioner pleads with this Court not to apply the foregoing rule to the instant case, for a rule on technicality should not defeat substantive justice. The BIR Commissioner apparently forgets that there are specific reasons why technical or procedural rules are imposed upon the courts, and that compliance with these rules, should still be the general course of action. Hence, this Court has expounded that -

> Procedural rules, we must stress, should be treated with utmost respect and due regard since they are designed to facilitate the adjudication of cases to remedy the worsening problem of delay in the resolution of rival claims and in the administration of justice. The requirement is in pursuance to the bill of rights inscribed in the Constitution which guarantees that "all persons shall have a right to the speedy disposition of their cases before all judicial, quasi-judicial and *administrative bodies*." The adjudicatory bodies and the parties to a case are thus enjoined to abide strictly by the rules. While it is true that a litigation is not a game of technicalities, it is equally true that every case must be prosecuted in accordance with the prescribed procedure to ensure an orderly and speedy administration of justice. There have been some instances