Republic of the Philippines
COURT OF TAX APPEALS
Quezon City

SECOND DIVISION

CHINA STATE PHILIPPINES CONSTRUCTION CORPORATION [Formerly: China State (Phils.) Construction Engineering Corporation), Petitioner,	**CTA Case No. 8522** **Members:** CASTAÑEDA, JR., *Chairperson* CASANOVA, *and* COTANGCO-MANALASTAS, *JJ.*
-versus-	
COMMISSIONER OF INTERNAL REVENUE, Respondent.	**Promulgated:** JUN 17 2016 4:30 p.m.

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DECISION

CASANOVA, *J.*:

This is a Petition for Review[1], filed on July 30, 2012 by petitioner China State Philippines Construction Corporation, seeking to (1) declare the Letter of Authority and the assessment arising therefrom as contained in the FAN dated June 28, 2009 as null and void; and (2) declare petitioner not liable for the following deficiency taxes and penalties, inclusive of interest and surcharges for taxable years 2003 to 2006:

a. Deficiency income tax in the aggregate amount of ₱129,601,451.47;

[1] Docket (Vol. I), pp. 1-36.

b. Deficiency VAT in the aggregate amount of ₱591,973,171.55; and

c. Deficiency EWT in the aggregate amount of ₱59,923,891.51.

The facts, as borne by the records, are as follows:

Petitioner China State Philippines Construction Corporation is a domestic corporation duly organized and existing under the laws of the Republic of the Philippines with Securities and Exchange Commission (SEC) Registration No. 167002[2] and with business address at Unit 1202 Summit One Tower, Shaw Blvd., Mandaluyong City.

On the other hand, respondent is the Commissioner of Internal Revenue, duly appointed to perform the duties of her office, including, *inter alia*, the power to decide disputed assessments, subject to the exclusive appellate jurisdiction of this Court pursuant to Section 4 of the Tax Code.[3]

China State Construction Engineering Corporation (CSCEC) is a foreign state-owned corporation organized and established under the laws of the People's Republic of China.[4]

On July 7, 1989, CSCEC was granted the Board of Investments (BOI) Certificate of Authority No. 1969[5], authorizing it to "establish a domestic subsidiary under the name of CHINA STATE (PHILS.) CONSTRUCTION ENGINEERING CORPORATION to engage in business as a contractor and supplier for public works projects funded or financed by the International Monetary Fund, World Bank, International Bank for Rural Reconstruction, Asian Development Bank and other international and regional lending institutions of which the People's Republic of China is a member state."

Pursuant thereto, petitioner was incorporated as a domestic subsidiary of CSCEC and registered with the SEC on August 14, 1989

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[2] Exhibit "I[4]".
[3] Par. 1, Facts Admitted in Respondent's Answer, Joint Stipulation of Facts and Issues (JSFI), Docket (Vol. I), p. 181.
[4] Par. 3, JSFI, Docket (Vol. I), p. 182.
[5] Exhibit "G[4]".

with total authorized capital stock of Eighty Million Pesos (₱80,000,000.00) consisting of 800,000 common shares with par value of ₱100.00 per share, of which 200,000 were issued and outstanding.[6] At the time of its incorporation, CSCEC owned 199,992 shares or 99% of petitioner.

Thereafter, CSCEC was awarded several contracts for internationally-funded public works project by the Philippine Government. Allegedly, as a wholly-owned subsidiary of CSCEC, petitioner assumed the responsibility of completing the projects awarded to CSCEC from August 14, 1989 to January 2006, since CSCEC was a non-resident foreign corporation without any branch in the Philippines.

Subsequently, the remaining authorized capital stock of 600,000 common shares of petitioner were subscribed by Filipino stockholders, reducing CSCEC's ownership over petitioner to 40% and finally to 25%.[7]

On January 12, 2006, CSCEC was granted a license to transact business in the Philippines and to establish a branch office with SEC License To Transact Business in the Philippines under Company Reg. No. FS200521059[8].

Petitioner was only able to independently obtain and was awarded contracts under its own name beginning July 2006. Thus, allegedly, for taxable year 2006, petitioner merely continued to undertake the completion of contracts awarded to CSCEC that it had begun to carry out in 2005 prior to the establishment of CSCEC's branch office.

On November 16, 2007, petitioner received a copy of the Letter of Authority (LOA) No. 21730[9] authorizing Revenue Officers Roberto J. delos Santos, Arlene F. Grageda, and Leandro E. Gabriel under the supervision of Jose Edimar P. Jaen to investigate and ascertain the internal revenue taxes of petitioner for taxable year 2006 and unverified prior years.[10]

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[6] Exhibit "I4".
[7] Exhibits "P4", "Q4" and "R4".
[8] Exhibit "G4".
[9] Exhibits "C4" and "1".
[10] Par. 4, JSFI, Docket (Vol. I), p. 182.

On May 25, 2011, petitioner received an undated Preliminary Assessment Notice[11], assessing it of deficiency income tax, value-added tax (VAT) and expanded withholding tax (EWT) for taxable years 2003 to 2006.

On October 3, 2011[12], petitioner received the Formal Letter of Demand with attached Details of Discrepancies and Formal Assessment Notices dated June 28, 2009[13] which sought to assess petitioner for the taxable years 2003 to 2006 the aggregate amount of Seven Hundred Eighty-One Million Four Hundred Ninety-Eight Thousand Five Hundred Fourteen and 53/100 (₱781,498,514.53) broken down as follows:

Taxable Year	Total Deficiency Income Tax	Total Deficiency VAT	Total Deficiency EWT	Total
2003	₱ 27,767,620.90		₱ 14,615,022.24	₱ 42,382,643.14
2004	45,884,171.83	194,713,071.24	17,751,123.94	258,348,367.01
2005	39,094,785.68	173,392,313.42	16,487,224.66	228,974,323.76
2006	16,854,873.06	223,867,786.89	11,070,520.67	251,793,180.62
TOTAL	**₱129,601,451.47**	**₱591,973,171.55**	**₱59,923,891.51**	**₱781,498,514.53**

The attached Details of Discrepancies merely provided for the following:

1. Disallowed Creditable Withholding Tax – All the 2% and 5% Creditable Withholding taxes were disallowed for failure to support the same and for the reason that your company is not the actual income recipient of the tax certificates. The Withholding Tax Certificates were issued in favor of China State Construction Engineering Corporation, a sister company who is the prime contractor of DPWH.

2. Expanded Withholding Tax - Being under the category of "Top 10,000 Corporations", you are hereby mandated under Revenue Regulations No. 17-03 to withhold and remit taxes in income payments made to supplier of goods and services.[14]

[11] Exhibit "16".
[12] Exhibit "A-1"
[13] Exhibits "A" and "17".
[14] Par. 6, JSFI, Docket (Vol. I), p. 182; and Exhibits "A" and "17".

On November 2, 2011[15], petitioner filed an administrative protest against the FAN by submitting to respondent a Protest Letter dated November 2, 2011[16]. Thereafter, on January 2, 2012[17], petitioner submitted all the documents in support of its protest in a Letter dated January 2, 2012[18].

In view of respondent's inaction on petitioner's administrative protest, petitioner filed the instant Petition for Review[19] on July 30, 2012.

Within the extended time granted by the Court[20], respondent filed her Answer[21] on October 4, 2012, and interposed the following special and affirmative defenses:

4. The tax deficiency assessment on the petitioner is based on facts, law, rules, and jurisprudence. Petitioner was assessed for tax deficiency on the ground that it is not the actual income recipient of the Withholding Tax Certificates, which were issued in favour of another taxpayer, which is China State Construction Engineering Corporation (CSCEC), a sister company who is the prime contractor of DPWH.

   4.1. Petitioner is liable for a total tax deficiency in the amount of P781,498,514.53 covering tax deficiency for the years 2003, 2004, 2005 and 2006 inclusive of surcharges and interest penalty. After verification and evaluation of the documents submitted by petitioner in protest to the final assessment notice, the documents failed to refute and cancel the assessments.

   4.2. A portion of the Memorandum dated February 22, 2011 contains the Audit Results and Findings of the investigating revenue officers. Pertinent portion of the Memorandum reads as follows:

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[15] Exhibit "B-2".
[16] Exhibit "B".
[17] Exhibit "C-2".
[18] Exhibit "C".
[19] Docket (Vol. I), pp. 1-36.
[20] Orders August 16, 2012, September 17, 2012 and October 2, 2012, Docket (Vol. I), pp. 105, 112, and 118.
[21] Docket (Vol. I), pp. 119-132.

Audit Results & Findings:

The total amount of Php745,750,097.38 has been determined to be the total Income Tax, VAT and EWT liabilities of the taxpayer for the taxable years 2003, 2004, 2005, and 2006. The assessment was based on the following:

1. All the 2% and 5% Creditable Withholding Taxes claimed for Income Tax and VAT, respectively, were disallowed for failure to substantiate the same for the years 2003, 2004, 2005. For taxable year 2006, the taxpayer was not the actual income recipient of the 5% tax certificates as proven by the certificates submitted by the taxpayer which were issued by the DPWH under the name of China State Construction Engineering Corporation. With regards to the 2% Creditable Withholding Tax claimed by the subject taxpayer, the examiner had no recourse but to disallow it for failure of China State (Phils.) to substantiate the same.

2. The taxpayer being under the category of "Top 10,000 Corporations" is mandated under Revenue Regulations No. 17-03 to withhold and remit taxes on income payments made to its suppliers of goods and services. The Undersigned have made use of the method of allocating and prorating the total expenses for the subject years based on the detailed expenses submitted by the taxpayer for the Third Quarter of 2006.

Deficiency Taxes for taxable year 2003:

	Income Tax	**EWT**
Basic Tax	9,164,231.32	4,745,137.09
50% Fraud Penalty	4,582,115.66	2,372,568.55

Interest till 3/15/11	12,676,881.18	
3/25/11		6,801,204.99
Total	24,423,228.16	13,918,910.63

The details for said assessments are explained as follows:

Income

The taxpayer is not the actual income recipient as reflected in the submitted certificates of Creditable Income Tax Withheld, hence, the withholding taxes claimed by it were disallowed.

Expanded Withholding Tax

The taxpayer failed to withhold and remit correctly the Expanded Withholding Taxes on the income payments made to its suppliers of goods and services. The EWT that should have been withheld and remitted is Php 6,348,779.28 but only Php641,905.99 was remitted and paid as deficiency tax for the regular investigation amounting to Php961,736.20.

<u>Deficiency Taxes for taxable year 2004:</u>

	Income Tax	**VAT**	**EWT**
Basic Tax	16,213,488.28	67,608,705.29	4,745,137.09
50% Fraud Penalty	8,106,744.14	33,804,352.65	3,081,792.35
Interest till 3/15/11	19,185,420.68		
3/25/10, 3/15/10		83,381,816.23	7,601,549.01
Total	43,505,653.10	184,794,874.17	16,846,926.06

The details for the above assessments are explained as follows:

Income Tax

The claimed 2% Creditable Withholding Tax was disallowed for the reason that the taxpayer was not able to support or present the certificates of the creditable withholding tax issued under its name.

Value-Added Tax

The amount of PhP67,808,705.29 claimed as 5% Creditable Withholding Tax from VAT was disallowed for the same reason as stated in the preceding paragraph.

Expanded Withholding Tax

The taxpayer failed to withhold taxes on income payments made to its suppliers of goods and services. The total basic amount of PhP6,163,584.70 of withholding taxes were not collected and remitted by the taxpayer.

<u>Deficiency Taxes for taxable year 2005</u>:

	Income Tax	**VAT**	**EWT**
Basic Tax	14,864,937.52	64,698,624.41	6,151,949.50
50% Fraud Penalty	7,432,468.76	32,349,312.21	3,075,974.75
Interest till 3/15/11	14,616,693.06		
3/25/11, 3/15/11		66,853,088.60	6,356,809.42
Total	36,914,099.34	163,901,025.22	15,584,733.67

The explanations for the above assessments are as follows:

Income Tax

Creditable Withholding Tax amounting to PhP15,099,565.00 was disallowed for the reason that the taxpayer was not able to support or present the certificates of withholding tax.

Value-Added Tax

The 5% Creditable Withholding Tax amounting to PhP64,752,666.72 was disallowed for the same reason as stated above.

Expanded Withholding Tax

The taxpayer failed to correctly withhold and remit the amount of PhP6,151,949.50 on income payments made to its suppliers of goods and services.

<u>Deficiency Taxes for taxable year 2006</u>:

	Income Tax	VAT	EWT
Basic Tax	6,936,161.75	90,269,268.91	7,456,402.41
50% Fraud Penalty	3,468,080.88	45,134,634.46	3,728,201.21
Interest till 3/15/11	5,433,095.50		
3/25/11, 3/15/11		66,853,088.60	6,356,809.42
Total	15,837,338.13	210,625,285.15	17,398,023.75

The above assessments are explained as follows:

Income Tax

Creditable Withholding Tax in the amount of PhP6,936,162.00 was disallowed for failure to present certificates of withholding tax. They submitted certificates of creditable withholding tax issued under the name of their sister company, China State Construction Engineering Corp.

Value-Added Tax

The whole amount of Creditable Withholding Tax amounting to PhP90,269,268.91 was disallowed for the reason that the taxpayer is not the recipient of the income payment made by DPWH.

Expanded Withholding Tax

The taxpayer failed to withhold and remit the amount of PhP7,456,402.41 on income payments to its suppliers of goods and services. Although as stated in the aforementioned statement of facts, the said amount was paid by the subject, without the concurrence of the RDO or the NID. The taxpayer is still liable for the payment of increments for its late payments.

Recommendations:

This is a clear case of tax fraud or evasion. The schemes perpetuated by the subject taxpayer in using the withholding tax certificates of another taxpayer (China State Construction Engineering Corporation) and its failure to withhold and remit taxes from income payments, which have resulted to a total deficiency tax of PhP745,750,097.38, have not only cause tremendous losses of revenues but also confirm the intent of the subject taxpayer in violating Sections 254 and 255 of the Tax Code.

5. Clearly, the deficiency assessments issued against petitioner have factual and legal bases.

5.1 On January 28, 2009, petitioner received a Notice of Informal Conference, informing it in this wise:

> Please be advised that the report of the investigation of your internal revenue tax liabilities for the years 2003-2006 was submitted by the investigating revenue officer under the Section Chief JOSE EDIMAR P. JAEN, for appropriate action.
>
> Pursuant to the provisions of Section 229 of the National Internal Revenue Code of 1997, which requires this Office to notify you of the

> findings on your tax liabilities and to enable you to present your side of the case, you are requested to appear for an informal conference...

5.2 Again, petitioner was issued a second notice of informal conference which was received by petitioner on January 13, 2011.

5.3 A Preliminary Assessment Notice (PAN) with an attached details of discrepancies was issued, which was received by petitioner on May 25, 2011. The total tax deficiency of the petitioner amounts to P781,498,514.53.

5.4 Attached to the above-mentioned PAN is the details of discrepancies, which provides as follows:

DETAILS OF DISCREPANCIES

Assessment No. _______

> 1. Disallowed Creditable Withholding Tax - All the 2% and 5% Creditable Withholding taxes were disallowed for failure to support the same and for the reason that your company is not the actual income recipient of the tax certificates. The Withholding Tax Certificates were issued in favor of China State Construction Engineering Corporation, a sister company who is the prime contractor of DPWH.
>
> 2. Expanded Withholding Tax - Being under the category of "Top 10,000 Corporations", you are hereby mandated under Revenue Regulations No. 17-03 to withhold and remit taxes on income payments made to supplier of goods and services.
>
> The records of this case disclosed that you have not introduced any evidence to overthrow the validity of our aid findings.

> It is requested that your aforesaid deficiency Income Tax and Value-Added Tax liabilities be paid immediately upon receipt hereof, inclusive of penalties incident to delinquency.

6. Based on the foregoing, the finding of deficiency tax liabilities against petitioner is proper in all respects. Worthy of note, are the words of the Supreme Court in the case of *Commissioner of Internal Revenue vs. Bank of Philippine Islands* (G.R. No. 134062, April 17, 2007)":

> 'Tax assessments by tax examiners are presumed correct and made in good faith. The taxpayer has the duty to prove otherwise. In the absence of proof of any irregularities in the performance of duties, an assessment duly made by a Bureau of Internal Revenue examiner and approved by his superior officers will not be disturbed. All presumptions are in favour of the correctness of tax assessments.'

7. Petitioner assailed the legality and validity of the Letter of Authority No. 2007 00021730. However, petitioner failed to consider that its case involves **tax fraud** which is way different from ordinary deficiency assessments. It can be noted that petitioner deliberately and intentionally used the Creditable Withholding Tax Certificates of another taxpayer, China State Construction Engineering Corporation. Such act is a clear showing of tax evasion. In connection thereto, the tax returns filed were fraudulent returns.

8. Petitioner sought to invalidate the LOA issued by taking refuge under the case of *Commissioner of Internal Revenue vs. Sony Philippines, Inc.* (G.R. No. 178697, 17 November 2010). Contrary, however, to the claim of the petitioner, the above-cited case is not applicable in the present case. It can be noted that the case cited by petitioner does not mention of the fraud, which is present in the instant case, there was no commission of fraud but not in the present case.

9. Assuming without conceding that petitioner indeed issued the LOA for taxable year 2006 and unverified prior year, the said LOA is valid since the fraud was discovered only in 2006. The rationale why respondent issued the LOA for 2006 and unverified prior years is that, she discovered the commission of fraud in the year 2006 and there is no way for her to ascertain as to the time when the tax fraud started to take place. Respondent cannot be faulted for its duty to investigate incidents when the taxpayer had a taxable income way higher than that which was reported, more so that the government is on the verge of losing hundreds millions of pesos.

10. Moreover, petitioner's assertion of prescription pursuant to Section 203 of the Tax Code is manifestly misplaced. It cannot be over emphasized that this case involves fraud and the applicable provision is Section 222 of the Tax Code, which provides:

> "SEC. 222. Exceptions as to period of Limitation of Assessment and Collection of Taxes. –
>
> (a) In the case of a **false or fraudulent return with intent to evade tax or failure to file a return**, the tax may be assessed, or a proceeding in court for the collection of such tax may be filed without assessment, at any time within **ten (10) years after the discovery of the falsify, fraud or omission**: Provided, That in a fraud assessment which has become final and executory, the fact of fraud shall be judicially taken cognizance of in the civil or criminal action for the collection thereof.

11. The assessment in the amount of P781,498,514.53 was issued in accordance with law and regulations.

12. Well-settled is the rule that tax assessments are entitled to the presumption of correctness and made in good faith. The taxpayer has the duty to prove otherwise. In the absence of proof of any irregularities in the

performance of duties, an assessment duly made by a Bureau of Internal Revenue examiner, and approved by his superior officers will not be disturbed. All presumptions are in favor of the correctness of tax assessments (*Sy Po vs. Court of Tax Appeals, 164 SCRA 524*). Dereliction on the part of petitioner to satisfactorily overcome the presumption of regularity and correctness of the assessment will justify the judicial upholding of said assessment notices."

The case was set for Pre-Trial Conference on October 25, 2012.[22] Accordingly, Respondent's Pre-Trial Brief[23] was filed on October 18, 2012, while petitioner's Pre-Trial Brief[24] was filed on October 22, 2012.

Trial ensued and, thereafter, the case was submitted for decision on July 20, 2015.

The parties jointly stipulated on the following issues[25] to be submitted for this Court's resolution, to wit:

A. Whether or not the Letter of Authority is valid.

B. Whether or not respondent's right to assess petitioner for deficiency taxes for the years 2003 to 2006 has already prescribed.

C. Whether or not petitioner is liable for the following:

i. Assessed deficiency income taxes and related surcharge and interest thereon for the taxable years 2003 to 2006, in the aggregate amount of Php129,601,451.47;

ii. Assessed deficiency VAT and related surcharge and interest thereon for the taxable year 2004 to

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[22] Notice of Pre-Trial Conference October 5, 2012, Docket (Vol. I), p. 133.
[23] Docket (Vol. I), pp. 137-143.
[24] Docket (Vol. I), pp. 144-158.
[25] JSFI, Docket (Vol. I), p. 183.

2006, in the aggregate amount of Php591,973,171.55; and

iii. Assessed deficiency expanded withholding tax and related surcharge and interest thereon for the taxable years 2003 to 2006, in the aggregate amount of Php59,923,891.51.

D. Whether or not the imposition of fifty percent (50%) penalty has legal and/or factual basis.

E. Whether or not the imposition of twenty percent (20%) interest has legal and/or factual basis.

The Letter of Authority is not valid. Accordingly, the deficiency tax assessments against petitioner for taxable years 2003 to 2005 are null and void.

Petitioner, citing the case of *Commissioner of Internal Revenue vs. Sony Philippines, Inc.*[26], contends that the Letter of Authority is void for covering audit of unverified prior years. Thus, it submits that the alleged deficiency taxes for taxable years 2003 to 2006 are null and void.

Respondent, on the other hand, argues that the above-cited case is not applicable in the present case on the ground that the instant case involves tax fraud, which is different from ordinary deficiency assessments. Respondent alleges that there is a clear showing of tax evasion when petitioner deliberately and intentionally used the Creditable Withholding Tax Certificates of another taxpayer, China State Construction Engineering Corporation. Moreover, respondent contends that she issued the LOA for 2006 and unverified prior years because she only discovered the commission of fraud in the year 2006 and there is no way for her to ascertain as to the time when the tax fraud started to take place.

[26] G.R. No. 178697, November 17, 2010.

It must be emphasized that before any revenue officer can conduct an examination or assessment, there must be a valid letter of authority.

Section 6 (A) of the National Internal Revenue Code (NIRC) of 1997, as amended, vests the Commissioner of Internal Revenue the power to authorize the examination of any taxpayer and the assessment of the correct amount of tax due, to wit:

> "SEC. 6. **Power of the Commissioner to Make Assessments and Prescribe Additional Requirements for Tax Administration and Enforcement.**
>
> (A)*Examination of Returns and Determination of Tax Due*. After a return has been filed as required under the provisions of this Code, **the Commissioner or his duly authorized representative may authorize the examination of any taxpayer and the assessment of the correct amount of tax**: *Provided, however*, That failure to file a return shall not prevent the Commissioner from authorizing the examination of any taxpayer." (*Emphasis ours*)

In relation thereto, Section 13 of the NIRC of 1997, as amended, provides that a Letter of Authority is the authority given to the appropriate revenue officer assigned to perform assessment functions. It empowers or enables said revenue officer to examine the books of account and other accounting records of a taxpayer for the purpose of collecting the correct amount of tax.[27] Section 13 provides:

> "SEC. 13. **Authority of a Revenue Officer**. - Subject to the rules and regulations to be prescribed by the Secretary of Finance, upon recommendation of the Commissioner, **a Revenue Officer assigned to perform assessment functions in any district may, pursuant to a Letter of Authority issued by the Revenue Regional Director, examine taxpayers within the jurisdiction of the district in order to collect the correct amount of tax, or to recommend**

[27] *Commissioner of Internal Revenue vs. Sony Philippines, Inc.*, G.R. No. 178697, November 17, 2010.

> **the assessment of any deficiency tax due** in the same manner that the said acts could have been performed by the Revenue Regional Director himself." (*Emphasis ours*)

Clearly, there must be a grant of authority before any revenue officer can conduct an examination or assessment. Equally important is that the revenue officer so authorized must not go beyond the authority given. In the absence of such an authority, the assessment or examination is a nullity.[28]

It must be noted that Section C of Revenue Memorandum Order (RMO) No. 43-90[29], provides that a letter of authority should cover a period not exceeding one taxable year. It also prohibits the practice of issuing Letters of Authority covering audit of "unverified prior years". Section 3 of RMO 43-90 reads:

> "C. Other policies for issuance of L/As.
>
> xxx xxx xxx
>
> 3. **A Letter of Authority should cover a taxable period not exceeding one taxable year. The practice of issuing L/As covering audit of "unverified prior years" is hereby prohibited.** If the audit of a taxpayer shall include more than one taxable period, the other periods or years shall be specifically indicated in the L/A." (*Emphasis ours*)

Moreover, in the case of *Commissioner of Internal Revenue vs. Sony Philippines, Inc.*[30], the Supreme Court also upheld the invalidity of the phrase "unverified prior years" in the Letter of Authority, because it violated Section C of RMO No. 43-90.

In the present case, the Letter of Authority No. 21730[31], dated November 13, 2007, allowed respondent to investigate and ascertain

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[28] *Ibid.*
[29] Amendment of Revenue Memorandum Order No. 37-90 Prescribing Revised Policy Guidelines for Examination of Returns and Issuance of Letters of Authority to Audit, dated September 20, 1990.
[30] G.R. No. 178697, November 17, 2010.
[31] Exhibit "C[4]".

the internal revenue taxes of petitioner indicated the period from taxable year 2006 and UPY (unverified prior years), to wit:

> "The bearers hereof, Rev. Officers Roberto J. delos Santos, Arlene F. Grageda, and Leandro E. Gabriel under the supervision of Jose Edimar P. Jaen of the National Investigation Division are authorized to examine your books of accounts and other accounting records for All Internal Revenue Taxes for the period from **Taxable years 2006 & UPY**. xxx" (*Emphasis ours*)

Clearly, the Letter of Authority No. 21730 is invalid having been issued in violation of Section C of RMO 43-90. Thus, the assessment conducted by respondent was unauthorized, because there was no valid Letter of Authority covering it.

A deficiency assessment issued without a valid authority is a nullity.[32] Considering that the Letter of Authority issued in this case authorized the audit for taxable year 2006 and "unverified prior years", which is prohibited, the deficiency income tax, VAT and EWT assessments for the taxable years 2003, 2004 and 2005 are null and void. Thus, the same must, therefore, be cancelled and set aside.

Respondent's right to assess petitioner for deficiency taxes for taxable year 2006 has already prescribed. Thus, the deficiency tax assessments against petitioner for taxable year 2006 is null and void.

Petitioner argues that it cannot be held liable for the alleged deficiency tax assessment because respondent's right to make such assessment has prescribed under Section 203 of the NIRC of 1997, as amended.

Respondent counters that petitioner's assertion of prescription pursuant to Section 203 of the Tax Code is manifestly misplaced. She contends that this case involves fraud and the applicable provision is Section 222 of the Tax Code. Respondent alleges that petitioner deliberately and intentionally used the Creditable

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[32] *People of the Philippines vs. Edwin T. So, Raymond R. Lee, Techpoint Computer Corporation*, CTA EB Crim. No. 028, March 6, 2010.

Withholding Tax Certificates of another taxpayer, CSCEC. She argues that such act is a clear showing of tax evasion and thus, the tax returns filed were fraudulent returns.

The Court finds merit in petitioner's argument.

Section 203 of the NIRC of 1997, as amended, mandates that respondent should make an assessment for deficiency taxes within three (3) years from the last day prescribed by law to file the tax return or the actual date of filing of such return, whichever comes later, to wit:

> "SEC. 203. **Period of Limitation Upon Assessment and Collection.** - Except as provided in Section 222, **internal revenue taxes shall be assessed within three (3) years after the last day prescribed by law for the filing of the return**, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period: *Provided*, That **in a case where a return is filed beyond the period prescribed by law, the three (3)-year period shall be counted from the day the return was filed.** For purposes of this Section, a return filed before the last day prescribed by law for the filing thereof shall be considered as filed on such last day."

Pursuant to Section 77 of the NIRC of 1997, as amended, a corporate taxpayer must file its annual income tax return on or before the fifteenth (15th) day of April. In this case, petitioner filed its Annual Income Tax Return for taxable year 2006 on April 13, 2007. Applying Section 203, respondent had until April 15, 2010 within which to assess petitioner for deficiency income tax for taxable year 2006.

With regard to VAT, Section 114 (A) of the NIRC, as amended, and Revenue Regulations (RR) No. 07-95, as amended by RR No. 08-02, requires that Quarterly VAT Returns be filed within twenty-five (25) days following the close of each taxable quarter. Below is the summary of the dates of filing of petitioner's Quarterly VAT Returns and the corresponding dates within which respondent should assess petitioner for deficiency VAT for the four quarters of taxable year 2006, to wit:

Taxable Quarter	Date Filed	Last Day to File Return	Last Day to Assess
1st Quarter (Original)	April 24, 2006[33]	April 25, 2006	April 25, 2009
1st Quarter (Amended)	July 25, 2007[34]	July 25, 2006	July 25, 2010
2nd Quarter (Original)	July 25, 2006[35]	July 25, 2006	July 25, 2009
2nd Quarter (Amended)	July 25, 2007[36]	July 25, 2006	July 25, 2010
3rd Quarter	October 25, 2006[37]	October 25, 2006	October 25, 2009
4th Quarter	January 25, 2007[38]	January 25, 2007	January 25, 2010

Insofar as EWT is concerned, Section 2.58(A)(2) of RR No. 2-98, as amended, by R.R. No. 06-01, provides that the return shall be filed on or before the tenth (10th) day of the month following the month in which withholding was made, except for taxes withheld for the month of December of each year, which shall be filed on or before January 15 of the succeeding year. The dates of the filing of petitioner's Monthly Remittance Return of Creditable Income Taxes Withheld (Expanded) as well as the last day for respondent to assess for deficiency EWT are summarized below:

Month Covered	Date Filed	Last Day to File Return	Last Day to Assess
January 2006	2/10/2006[39]	2/10/2006	2/10/2009
February 2006	3/10/2006[40]	3/10/2006	3/09/2009
March 2006	4/10/2006[41]	4/10/2006	4/10/2009
April 2006	5/10/2006[42]	5/10/2006	5/11/2009[43]
May 2006	6/13/2006[44]	06/13/06[45]	06/15/09[46]
June 2006	7/10/2006[47]	7/10/2006	7/10/2009

[33] Exhibits "U", "U-1" and "U-2".
[34] Exhibits "X", "X-1" and "X-2".
[35] Exhibits "W", "W-1" and "W-2".
[36] Exhibits "X", "X-1" and "X-2".
[37] Exhibits "Y", "Y-1" and "Y-2".
[38] Exhibits "Z", "Z-1" and "Z-2".
[39] Exhibits "OOO", "OOO-1" and "OOO-2".
[40] Exhibits "PPP", "PPP-1" and "PPP-2".
[41] Exhibits "QQQ", "QQQ-1" and "QQQ-2".
[42] Exhibits "RRR", "RRR-1" and "RRR-2".
[43] May 10, 2009 fell on a Sunday.
[44] Exhibits "SSS", "SSS-1" and "SSS-2".
[45] June 10, 2006 fell on a Saturday and June 12, 2006 is a holiday.
[46] June 13, 2009 fell on a Saturday.
[47] Exhibits "TTT", "TTT-1" and "TTT-2".

July 2006	8/10/2006[48]	8/10/2006	8/10/2009
August 2006	9/11/2006[49]	9/11/2006[50]	9/11/2009
September 2006	10/10/2006[51]	10/10/2006	10/12/2009[52]
October 2006	11/10/2006[53]	11/10/2006	11/10/2009
November 2006	12/11/2006[54]	12/11/2006[55]	12/11/2009
December 2006	1/15/2007[56]	1/15/2007	1/15/2010

Therefore, the last day for respondent to issue an assessment for taxable year 2006 was on April 15, 2010 for income tax, on July 25, 2010 at the latest for VAT, and on January 15, 2010 at the latest for EWT.

In this case, while the Formal Letter of Demand[57] is dated June 28, 2009, the Court cannot consider the same as the date when the assessment was made considering that some of the memoranda, letters and notices that are part of investigation prior to the issuance of the Formal Letter of Demand and Final Assessment Notice were dated after June 28, 2009, to wit:

1. Memorandum for the Deputy Commissioner, Legal and Inspection Group[58] dated February 22, 2010 recommending the issuance of the Preliminary Assessment Notice;
2. Notice of Informal Conference[59] inviting petitioner an informal conference on January 17, 2011;
3. Letter[60] September 29, 2010 requesting the DPWH to furnish the National Investigation Division (NID) of BIR of the enumerated certifications and documents stated therein; and

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[48] Exhibits "UUU", "UUU-1" and "UUU-2".
[49] Exhibits "VVV", "VVV-1" and "VVV-2".
[50] September 10, 2006 fell on a Sunday.
[51] Exhibits "WWW", "WWW-1", "WWW-2", "WWW-3" and "WWW-4".
[52] October 10, 2009 fell on a Saturday.
[53] Exhibits "XXX", "XXX-1" and "XXX-2".
[54] Exhibits "YYY", "YYY-1" and "YYY-2".
[55] December 10, 2006 fell on a Sunday.
[56] Exhibits "ZZZ", "ZZZ-1" and "ZZZ-2".
[57] Exhibits "A" and "17".
[58] Exhibit "15".
[59] Exhibit "14".
[60] Exhibit "12".

4. Letters[61] dated July 23, 2010 requesting the DPWH to furnish the NID of BIR of the enumerated certifications and documents stated therein.

The Supreme Court, in the case of *Barcelon Roxas Securities, Inc. vs. Commissioner of Internal Revenue*[62], held that assessment is made within the prescriptive period if notice to this effect is released, mailed or sent by the CIR to the taxpayer within said period, to wit:

> "Under Section 203 of the National Internal Revenue Code (NIRC), respondent had three (3) years from the last day for the filing of the return to send an assessment notice to petitioner. In the case of *Collector of Internal Revenue v. Bautista*, this Court held that an **assessment is made within the prescriptive period if notice to this effect is released, mailed or sent by the CIR to the taxpayer within said period. Receipt thereof by the taxpayer within the prescriptive period is not necessary.** At this point, it should be clarified that the rule does not dispense with the requirement that the taxpayer should actually receive, even beyond the prescriptive period, the assessment notice which was timely released, mailed and sent." (*Emphasis ours*)

A perusal of the Formal Letter of Demand shows that the same was served to petitioner through personal service on October 3, 2011[63]. Thus, the assessment against petitioner for taxable year 2006 is considered made on October 3, 2011 when respondent sent the Formal Letter of Demand to petitioner through personal service.

Considering that the latest date that respondent can validly assess petitioner for taxable year 2006 is April 15, 2010 for income tax, July 25, 2010 for VAT, and January 15, 2010 for EWT, it is evident that respondent no longer has the right to assess petitioner for any internal revenue taxes for taxable year 2006 when she made the assessment against petitioner on October 3, 2011.

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[61] Exhibit "11".
[62] G. R. No. 157064, August 7, 2006.
[63] Exhibit "A-1".

Now, as to respondent's contention that the applicable provision in this case is Section 222 of the NIRC of 1997, as amended, the Court disagrees.

Section 222 (a) of the NIRC of 1997, as amended, reads:

> "**SEC. 222.** ***Exceptions as to Period of Limitation of Assessment and Collection of Taxes.*** —
>
> (a) **In the case of a false or fraudulent return with intent to evade tax or of failure to file a return, the tax may be assessed, or a proceeding in court for the collection of such tax may be filed without assessment, at any time within ten (10) years after the discovery of the falsity, fraud or omission**: *Provided*, That in a fraud assessment which has become final and executory, the fact of fraud shall be judicially taken cognizance of in the civil or criminal action for the collection thereof.

The above provision enumerates three (3) instances when the running of the three-year prescriptive period does not apply, to wit: (1) filing a false return, (2) filing a fraudulent return with intent to evade tax, and (3) failure to file a return. In all these instances, the period within which to assess deficiency taxes is ten (10) years from discovery of the fraud, falsification or omission.

The Supreme Court held in the case of *Jose B. Aznar vs. Court of Tax Appeals and Collector of Internal Revenue*[64] that the abovementioned provision should be interpreted to mean a separation of the three different situations of false return, fraudulent return with intent to evade tax, and failure to file a return; which is strengthened immeasurably by the last portion of the provision that segregates the situations into three different classes, namely "falsity", "fraud" and "omission". That there is a difference between "false return" and "fraudulent return" cannot be denied. While the first merely implies deviation from the truth, whether intentional or not, the second implies intentional or deceitful entry with intent to evade the taxes due.

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[64] G.R. No. L-20569, August 23, 1974.

Respondent alleges that the returns filed by petitioner for taxable year 2006 are fraudulent returns. However, she failed to present any evidence to substantiate her claim.

It must be stressed that the existence of fraud is never presumed but must be proven by clear and convincing evidence. In the case of *Petron Corporation vs. Commissioner of Internal Revenue*[65] the Supreme Court, held "that fraud is a question of fact which cannot be presumed and must be proven by clear and convincing evidence by the party alleging the same."

Moreover, in the Aznar case, fraud in relation to the filing of income tax return, was discussed in this manner:

> "xxx. **The fraud contemplated by law is actual and not constructive. It must be intentional fraud, consisting of deception willfully and deliberately done or resorted to in order to induce another to give up some legal right. Negligence, whether slight or gross, is not equivalent to the fraud with intent to evade the tax contemplated by the law. It must amount to intentional wrong-doing with the sole object of avoiding the tax.** It necessarily follows that a mere mistake cannot be considered as fraudulent intent, and if both petitioner and respondent Commissioner of Internal Revenue committed mistakes in making entries in the returns and in the assessment, respectively, under the inventory method of determining tax liability, it would be unfair to treat the mistakes of the petitioner as tainted with fraud and those of the respondent as made in good faith.

In this case, respondent contends that petitioner used the Creditable Withholding Tax Certificates of its sister company, CSCEC. She argues that such act is a clear showing of tax evasion and thus, the tax returns filed by petitioner were fraudulent returns.

However, a perusal of the records shows that respondent failed to present any evidence to prove that the act of petitioner in using the Creditable Withholding Tax Certificates of CSCEC shows its intent to evade tax.

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[65] G.R. No. 180385, July 28, 2010.

In the case of *Commissioner of Internal Revenue vs. The Estate of Benigno P. Toda Jr.*[66] the Supreme Court held that "tax evasion connotes the integration of three factors: (1) the end to be achieved, i.e., the payment of less than that known by the taxpayer to be legally due, or the non-payment of tax when it is shown that a tax is due; (2) an accompanying state of mind which is described as being evil, in bad faith, willfull, or deliberate and not accidental; and (3) a course of action or failure of action which is unlawful."

Respondent failed to prove that petitioner and CSCEC are sister companies and that petitioner is not allowed to use the Creditable Withholding Tax Certificates of CSCEC. More importantly, she failed to present any evidence that would show that the returns filed by petitioner for taxable year 2006 are fraudulent returns which would warrant the application of Section 222 of the NIRC of 1997, as amended.

It must be kept in mind that the very reason why the law provided for prescription is to give taxpayers peace of mind, that is, to safeguard them from unreasonable examination, investigation, or assessment. The law on prescription, being a remedial measure, should be liberally construed in order to afford such protection. As a corollary, the exceptions to the law on prescription should perforce be strictly construed.[67]

Considering that petitioner CIR failed to substantiate her allegation by clear and convincing proof that petitioner filed fraudulent returns for taxable year 2006, the three (3)-year period prescribed by law to issue an assessment was therefore not extended. The assessment issued by respondent against petitioner for taxable year 2006 is therefore void for being issued beyond the three-year prescriptive period under Section 203 of the NIRC of 1997, as amended.

Finding that the assessments for taxable years 2003, 2004 and 2005 are void for being issued without a valid authority and the assessment for taxable year 2006 also void for being issued when

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[66] G.R. No. 147188, September 14, 2004.

[67] *Commissioner of Internal Revenue vs. Standard Chartered Bank,* G.R. No. 192173, July 29, 2015.

respondent's right to assess petitioner has already prescribed, the Court finds it no longer necessary to discuss the other issues raised.

WHEREFORE, premises considered, the instant Petition for Review is **GRANTED**. Considering that respondent had no valid authority to assess petitioner for taxable years 2003, 2004 and 2005 and her right to assess petitioner for taxable year 2006 has already prescribed, the assessment against petitioner dated June 28, 2009 for deficiency income tax, VAT and EWT in the aggregate amount of Seven Hundred Eighty-One Million Four Hundred Ninety-Eight Thousand Five Hundred Fourteen and 53/100 (₱781,498,514.53) for taxable years 2003 to 2006 is **CANCELLED** and deemed **WITHDRAWN**.

SO ORDERED.

CAESAR A. CASANOVA
Associate Justice

WE CONCUR:

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Associate Justice

(On Leave)
AMELIA R. COTANGCO-MANALASTAS
Associate Justice

ATTESTATION

I attest that the conclusions in the above Decision were reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Associate Justice
Chairperson, Second Division

CERTIFICATION

Pursuant to Article VIII, Section 13 of the Constitution, and the Division Chairperson's Attestation, it is hereby certified that the conclusions in the above Decision were reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

ROMAN G. DEL ROSARIO
Presiding Justice