REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

SPECIAL FIRST DIVISION

JOWELLE'S AUTO PARTS, INC., *Petitioner,*

-*versus*-

BUREAU OF INTERNAL REVENUE, *Respondent.*

CTA Case No.10018

Members:

DEL ROSARIO, *P.J., Chairperson,*
MANAHAN, *and*
REYES-FAJARDO, *JJ.*

Promulgated:

OCT 05 2023; 3:00PM

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D E C I S I O N

MANAHAN, *J.:*

This is a *Petition for Review with Motion to Suspend Collection of Taxes* filed by Jowelle's Auto Parts, Inc. against respondent Bureau of Internal Revenue (BIR) on February 1, 2019, praying that judgment be rendered ordering respondent to: a.) lift the Warrant of Distraint and/or Levy (WDL) No. 2019-00005 dated January 30, 2019; b.) declare void the Preliminary Assessment Notice (PANs), Formal Letters of Demand (FLDs) and Preliminary Collection Letter (PCL); and, c.) issue an order to suspend collection of taxes for taxable years (TYs) 2011, 2012, and 2013.[1]

THE PARTIES

Petitioner Jowelle's Autoparts, Inc. is a corporation with principal address at Cabatuan Road, San Fermin, Cauayan City, Isabela.[2]

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[1] Statement of the Case, Pre-Trial Order dated October 21, 2019, Docket – Vol. I, p. 393.
[2] Par. 1, The Parties, *Petition for Review,* Docket – Vol. I, p. 12.

Respondent, BIR is a government agency with postal address at 7th Floor BIR Bldg., BIR Road, Quezon City.[3]

THE FACTS

On June 13, 2014, petitioner received respondent's Letter of Authority (LOA) No. 015-2014-00000007 for TY 2011,[4] LOA No. 015-2014-00000008 for TY 2012,[5] and LOA No. 015-2014-00000009 for TY 2013[6].[7]

Petitioner received respondent's PAN dated April 6, 2015, for TY 2013 on April 14, 2015, finding petitioner liable for the following deficiency taxes:[8]

Income tax	₱31,314,902.15
Value-added tax	₱11,706,293.65
TOTAL	₱43,021,195.80

On April 22, 2015, petitioner received respondent's PAN dated February 16, 2015 for TY 2011,[9] and PAN dated April 10, 2015 for TY 2012,[10] finding petitioner liable for income tax, value added tax (VAT), improperly accumulated earnings tax (IAET), and registration fee, detailed as follows:[11]

	Taxable year	Income tax	VAT	IAET	Registration fee	Total
For the PAN dated February 6, 2015	2011	₱42,981,980.92	₱16,986,092.87	₱16,138,086.48	₱4,676.39	₱76,020,836.66
For the PAN dated April 10, 2015	2012	₱40,879,465.30	₱13,770,119.53	₱14,110,316.00		₱68,759,901.55

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[3] Par. 1, Joint Stipulation of Facts, *Joint Stipulation of Facts and Issues* (JSFI), Docket – Vol. I, p. 382.
[4] Exhibits "P-1" and "R-1", BIR Records (Folder 1 of 4), p. 2.
[5] Exhibits "P-2" and "R-19", BIR Records (Folder 3 of 4), p. 345.
[6] Exhibits "P-3" and "R-10", BIR Records (Folder 2 of 4), p. 118.
[7] Par. 3, Joint Stipulation of Facts, JSFI, Docket – Vol. I, p. 382.
[8] Par. 4, Joint Stipulation of Facts, JSFI, Docket – Vol. I, p. 382; Exhibits "R-15" to "R-15-A" and "P-4", BIR Records (Folder 2 of 4), pp. 580 to 583.
[9] Exhibits "R-6" to "R-6-A", BIR Records (Folder 1 of 4), pp. 265 to 269.
[10] Exhibits "R-24" to "R-24-A", BIR Records (Folder 3 of 4), pp. 475 to 478.
[11] Pars. 5 and 6, Joint Stipulation of Facts, JSFI, Docket – Vol. I, p. 383. *om*

Thereafter, on June 25, 2015, petitioner received three (3) FLDs, all dated June 22, 2015, for TYs 2011,[12] 2012,[13] and 2013,[14] finding petitioner liable for the following deficiency taxes:[15]

	Taxable year	Income tax	VAT	IAET	Registration fee	Total
For the FLD dated June 22, 2015	2011	₱44,338,164.91	₱17,546,660.63	₱16,669,277.42	₱4,851.39	₱78,558,954.36
For the FLD dated June 22, 2015	2012	₱41,750,764.86	₱14,056,915.17	₱14,404,197.78		₱70,211,877.81
For the FLD dated June 22, 2015	2013	₱32,095,207.91	₱11,469,857.44			₱43,565,065.35

In reply to the said FLDs, petitioner filed three (3) Legal Petition Notices dated July 10, 2015 on July 24, 2015, as its protest/request for reinvestigation.[16]

Subsequently, petitioner filed another three (3) Legal Petition Notices dated August 14, 2015 for TYs 2011, 2012 and 2013 on September 22, 2015, as its supplemental protest for reinvestigation, submitting therein additional documents to support its claim.[17]

On July 11, 2018, petitioner received respondent's PCL dated July 9, 2018, requesting the latter to pay its tax liabilities for TYs 2011, 2012 and 2013.[18]

Petitioner, thereafter, submitted to respondent another Legal Petition Notice dated July 13, 2018 on July 16, 2018.[19]

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[12] Exhibits "R-7" to "R-7-B", BIR Records (Folder 1 of 4), pp. 272 to 279.
[13] Exhibits "R-25" to "R-25-B", BIR Records (Folder 3 of 4), pp. 481 to 494.
[14] Exhibits "R-16" to "R-16-B", BIR Records (Folder 2 of 4), pp. 594 to 599.
[15] Pars. 7, 8 and 9, JSFI, Docket – Vol. I, p. 383.
[16] Exhibit "P-10", Docket – Vol. II, pp. 697 to 705; Exhibit "P-10-A", Docket – Vol. II, pp. 706 to 713; Exhibit "P-10-B", Docket – Vol. II, pp. 714 to 719.
[17] Exhibit "P-11", Docket – Vol. II, pp. 720 to 749; Exhibit "P-12", Docket – Vol. II, pp. 750 to 787; and Exhibit "P-13", Docket – Vol. II, pp. 788 to 829.
[18] Exhibits "R-29" and "P-14", BIR Records (Folder 4 of 4), pp. 1 to 2.
[19] Exhibit "P-15", Docket – Vol. II, pp. 830 to 842.

Respondent then issued the Final Notice Before Seizure (FNBS) dated January 15, 2019,[20] followed by WDL No. 2019-00005 dated January 30, 2019, which petitioner respectively received on January 17, 2019 and January 31, 2019.[21]

Respondent then issued Warrants of Garnishment to the following banks: (1) Philippine National Bank; (2) Landbank of the Philippines; (3) Rizal Commercial Banking Corporation; (4) Metropolitan Bank & Trust Company; (5) BDO Unibank, Inc.; (6) Development Bank of the Philippines; (7) UnionBank of the Philippines; (8) China Banking Corporation; and, (9) Bank of the Philippine Islands.[22]

On February 1, 2019, petitioner filed the present Petition for Review with Motion to Suspend Collection of Taxes, praying for this Court to: (1) lift respondent's WDL No. No. 2019-00005 dated January 30, 2019; (2) declare void respondent's PANs, FLDs, and PCL; and, (3) issue an Order suspending the collection of taxes.[23]

The hearing on petitioner's Motion to Suspend Collection of Taxes was initially set on March 7, 2019.[24] However, petitioner filed a Very Urgent Motion to Reset (Scheduled Hearing on 7 March 2019) on March 4, 2019,[25] praying that its motion be granted and that an Order be issued resetting the hearing thereon on April 19, 2019 or April 2, 2019. There being no objection on the part of respondent's counsel, the hearing on petitioner's Motion to Suspend Collection of Taxes was reset to April 2, 2019 during the hearing held on March 7, 2019.[26]

On April 1, 2019, petitioner filed another Very Urgent Motion to Reset,[27] praying that the Court reset the April 2, 2019 hearing. However, during the April 2, 2019 hearing, respondent's counsel objected to petitioner's Very Urgent Motion to Reset on the ground that this was the second request

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[20] Exhibit "R-30", BIR Records (Folder 4 of 4), p. 33.
[21] Exhibits "P-16" and "R-31", BIR Records (Folder 4 of 4), p. 35; Par. 2, Joint Stipulation of Facts, JSFI, Docket – Vol. I, p. 382.
[22] Exhibits "R-32" to "R-40", BIR Records (Folder 4 of 4), pp. 40, 42, 45, 46, 49, 50, 52, 54 and 56, respectively.
[23] Docket – Vol. I, pp. 12 to 19.
[24] *Notice of Hearing (Motion to Suspend Collection of Taxes)* dated February 26, 2019, Docket – Vol. I, p. 218.
[25] Docket – Vol. I, pp. 220 to 222.
[26] Minutes of the hearing held on, and Order dated, March 7, 2019, Docket – Vol. I, pp. 224 to 227.
[27] Docket – Vol. I, pp. 237 to 238. *cm*

for a resetting of hearing. Finding merit thereon, the Court denied both petitioner's Very Urgent Motion to Reset and Motion to Suspend Collection of Taxes.[28]

Respondent filed his Answer on April 15, 2019.[29]

Respondent transmitted the BIR Records of the case consisting of four (4) folders on April 25, 2019.[30]

In the Resolution dated May 3, 2019,[31] the case was referred to mediation at the Philippine Mediation Center – Court of Tax Appeals (PMC-CTA), and the parties were ordered to immediately proceed and to personally appear or through their authorized representatives before Ms. Avigail B. Sanchez, Mediation Staff Assistant. However, both parties failed to agree to enter into mediation proceedings before the PMC-CTA, and thus, the Pre-Trial Conference was scheduled, and held on August 15, 2019.[32] Prior thereto, Respondent's Pre-Trial Brief was filed on August 6, 2019;[33] while Petitioner's Pre-Trial Brief was submitted on August 13, 2019.[34]

On September 16, 2019, the parties submitted their Joint Stipulation of Facts and Issues,[35] which was approved in the Resolution dated October 7, 2019,[36] thereby deeming the termination of the Pre-Trial. Subsequently, the Pre-Trial Order dated October 21, 2019 was issued.[37]

During the trial of this case, petitioner offered the testimonies of the following individuals, namely: (1) Ms. Divine Grace Fresco,[38] petitioner's Tax Consultant; and (2) Mr.

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[28] Minutes of the hearing held on, and Order dated, April 2, 2019, Docket – Vol. I, pp. 240 to 243.
[29] Docket – Vol. I, pp. 245 to 258.
[30] Docket – Vol. I, pp. 260 to 262.
[31] Resolution dated May 3, 2019, Docket – Vol. I, pp. 270 to 271.
[32] Resolution dated July 8, 2019, Docket – Vol. I, p. 279; Notice of Pre-Trial Conference dated July 15, 2019, Docket – Vol. I, pp. 280 to 281; Minutes of the hearing held on, and Order dated, August 15, 2019, Docket – Vol. I, pp. 356 to 358, and 361 to 363, respectively.
[33] Docket – Vol. I, pp. 287 to 292.
[34] Docket – Vol. I, pp. 351 to 355.
[35] Docket – Vol. I, pp. 382 to 387.
[36] Docket – Vol. I, p. 390.
[37] Docket – Vol. I, pp. 393 to 401.
[38] Exhibit "P-17", Docket – Vol. I, pp. 341 to 350; Minutes of the hearing held on, and Order dated, November 12, 2019, Docket – Vol. I, pp. 426 to 429.

Franklin R. Casedo,[39] the Court-commissioned Independent Certified Public Accountant (ICPA).[40]

On December 12, 2019, respondent filed a Motion for Early Resolution on the Issue of Jurisdiction of the Honorable Court,[41] praying that the same be given due course and that the instant petition be dismissed for being time barred and/or lack of jurisdiction. Petitioner posted its Comment (to Issue of Jurisdiction) on December 16, 2019.[42] In the Resolution dated January 30, 2020,[43] the Court denied respondent's Motion for Early Resolution on the Issue of Jurisdiction.

The ICPA's Report was submitted to the Court on May 25, 2021.[44]

Thereafter, Petitioner's Formal Offer of Evidence was filed on October 21, 2021.[45] Respondent submitted his Comment (on Petitioner's Formal Offer of Evidence) on November 18, 2021.[46] In the Resolution dated March 17, 2022,[47] the Court admitted petitioner's offered exhibits, except for Exhibits "P-10-A" and "P-10-B", for failure to identify.

For its part, respondent offered the testimonies of his employees, namely: (1) Ms. Pamela Español,[48] Revenue Officer (RO) III of Revenue Region (RRgn) No. 3; (2) Ms. Jedaya C. Duran,[49] RO II of RRgn No. 3, Collection Division; (3) Ms. Zarah Rosanna Dumaga,[50] RO III of the Assessment Section, Revenue District Office (RDO) No. 13, Tuguegarao City; and (4) Ms.

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[39] Exhibit "P-21", Docket – Vol. II, pp. 652 to 657; Minutes of the hearing held on, and Order dated, July 6, 2021, Docket – Vol. II, pp. 658 to 662; Minutes of the hearing held on, and Order dated, October 7, 2021, Docket – Vol. II, pp. 683 to 686.

[40] *Oath of Commission* dated February 11, 2021, Docket – Vol. II, p. 575-C; Minutes of the hearing held on, and Order dated, February 11, 2021, Docket – Vol. II, pp. 575 to 575-B, and 576 to 576-A, respectively

[41] Docket – Vol. I, pp. 434 to 443.

[42] Docket – Vol. I, pp. 452 to 454.

[43] Docket – Vol. I, pp. 469 to 471.

[44] Exhibit "P-22", Docket – Vol. II, pp. 599 to 646.

[45] Docket – Vol. II, pp. 691 to 695.

[46] Docket – Vol. II, pp. 843 to 845.

[47] Docket – Vol. II, pp. 854 to 855.

[48] Exhibit "R-42", Docket – Vol. I, pp. 298 to 305; Order dated May 12, 2022, Docket – Vol. II, pp. 857 to 857-A.

[49] Exhibit "R-45", Docket – Vol. I, pp. 310 to 316; Order dated May 26, 2022, Docket – Vol. II, pp. 859 to 859-A.

[50] Exhibit "R-43, Docket – Vol. I, pp. 321 to 328; Order dated May 12, 2022, Docket – Vol. II, pp. 857 to 857-A. cm

Elizabeth C. Soriano,[51] Chief Revenue Officer III of RRgn No. 3, and Assistant Revenue District Officer of RDO No. 15 - Naguilian.

On June 3, 2022, respondent filed his Formal Offer of Evidence.[52] Petitioner then posted its Comment (to Formal Offer of Evidence) on June 16, 2022.[53] In the Resolution dated August 10, 2022,[54] the Court admitted respondent's exhibits.

Respondent filed his Memorandum on September 15, 2022,[55] while Petitioner's Memorandum was submitted on September 16, 2022.[56]

This case was submitted for decision on October 6, 2022.[57]

THE ISSUES

The parties submitted the following issues for the Court's resolution, to wit:

> "1. Whether or not this Honorable Court has jurisdiction over the instant case; and
>
> In the alternative, should the Court assume jurisdiction:
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> 2. Whether or not the Petitioner is liable for the assessed deficiency taxes for TYs 2011, 2012, and 2013 in the amounts of Php 78,558,954.36, Php70,211,877.81, and Php43,565,065.35, respectively."[58]

Petitioner's arguments:

Petitioner argues that without the issuance of a Final Decision on Disputed Assessment (FDDA) on its protest filed

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[51] Exhibit "R-44", Docket – Vol. I, pp. 333 to 340; Order dated May 26, 2022, Docket – Vol. II, pp. 859 to 859-A.
[52] Docket – Vol. II, pp. 860 to 871.
[53] Docket – Vol. II, pp. 875 to 878.
[54] Docket – Vol. II, pp. 881 to 882.
[55] Docket – Vol. II, pp. 884 to 912.
[56] Docket – Vol. II, pp. 914 to 921.
[57] Minute Resolution dated October 6, 2022, Docket – Vol. III, p. 922.
[58] Joint Statement of Issues To Be Tried or Resolved, JSFI, Docket – Vol. I, p. 384.

against the FLD/FANs, the WDL No. 2019-0005 dated January 30, 2019 issued by respondent is premature, hence void. Alternatively, should the PCL dated July 9, 2018 be treated as respondent's FDDA, the same would still be void for it did not state the factual and legal bases for the assessment. Petitioner observes that the basic taxes described in the FLDs and the PCL are exactly the same despite its protest and submission of additional supporting documents. Citing the case of *Commissioner of Internal Revenue vs. Unioil Corporation,* [59] petitioner alleges that the failure of respondent to give due consideration to the arguments and evidence submitted by the taxpayer in its protest, renders the assessment void. Petitioner claims that respondent failed to consider the accounting records and documents submitted in its protest in violation of its right to due process.

On the substantive merits of the deficiency tax assessments, petitioner contends that the undeclared purchases and expenses do not necessarily result to undeclared income and that these alleged disallowed and unsupported expenses and purchases were already supported by its submission of sales invoices, purchase forms, order slips, delivery receipts etc. when it filed its Legal Petition (protest) dated August 14, 2015.

Respondent's counter-arguments:

Respondent initially challenges the jurisdiction of the Court over the instant Petition for Review as it argues that no appeal was made by petitioner within the thirty (30)-day period from receipt of the PCL. This is based on the theory of respondent that the PCL is considered the FDDA because it already clearly states that the tax deficiency is due and payable and contains a statement that if left unpaid, the BIR shall thereafter enforce collection through administrative summary remedies. It cites various jurisprudence that supposedly recognized that letters expressing intent to enforce collection despite taxpayers' protests may also be considered as the final decision of the Commissioner of Internal Revenue (CIR) appealable to the Court. Respondent avers that petitioner neither appealed the contents of the PCL to the CIR and filed the instant Petition for Review with the Court beyond the thirty (30)-day period prescribed by the law.

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[59] G.R. No. 204405, August 4, 2021.

Respondent further insists that the deficiency tax assessments against petitioner for TYs 2011, 2012 and 2013 are correct because it was found that petitioner failed to declare the correct purchases and failed to support some of its claimed expenses with sufficient documentation. Respondent also mentions that petitioner did not register some of its books of accounts and/or failed to make proper recordings therein. In addition, respondent alleges that petitioner was found to be liable for IAET for TYs 2011 and 2012 for retaining earnings that far exceed the reasonable needs of the business. Finally, respondent states that petitioner was found to be liable for the payment of the annual registration fee for 2011.

THE RULING OF THE COURT

The Court finds the present Petition for Review partly meritorious.

On the issue of jurisdiction

Petitioner argues that the issuance of WDL No. 2019-00005 dated January 30, 2019 by respondent was premature because it was issued without the issuance of an FDDA, despite the filing of petitioner's protest.

On the other hand, respondent insists that the thirty (30)-day period within which to file a Petition for Review before this Court should be counted from the date of the receipt of the PCL on July 11, 2018, as the same was the earliest opportunity for petitioner to question the denial of its protest. But since the present Petition was only filed on February 1, 2019 or beyond the thirty (30)-day period provided by law, the Court has no jurisdiction over the instant Petition for Review.

The Court finds both arguments without merit.

Respondent's argument must fail in the light of Section 7(a)(1) of Republic Act (RA) No. 1125,[60] as amended by RA No. 9282,[61] which confers upon this Court the jurisdiction to decide

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[60] AN ACT CREATING THE COURT OF TAX APPEALS.
[61] AN ACT EXPANDING THE JURISDICTION OF THE COURT OF TAX APPEALS (CTA), ELEVATING ITS RANK TO THE LEVEL OF A COLLEGIATE COURT WITH SPECIAL JURISDICTION AND ENLARGING ITS MEMBERSHIP, AMENDING FOR THE PURPOSE

not only cases on disputed assessments and refunds of internal revenue taxes, but also on "other matters" arising under the 1997 National Internal Revenue Code (NIRC), as amended. Said provision reads:

> "SEC. 7. *Jurisdiction.* – The CTA shall exercise:
>
> (a) Exclusive appellate jurisdiction to review by appeal, as herein provided:
>
> (1) **Decisions of the Commissioner of Internal Revenue in cases involving disputed assessments, refunds of internal revenue taxes**, fees or other charges, penalties in relation thereto, or **other matters arising under the National Internal Revenue Code or other laws administered by the Bureau of Internal Revenue;"** *(Emphases supplied)*

Based on the foregoing provision, it is clear that the appellate jurisdiction of this Court is not limited to cases which involve decisions of the CIR, [62] on matters relating to assessments or refunds. The second part of the provision covers other cases that arise out of the NIRC or related laws administered by respondent.[63]

In *Philippine Journalists, Inc. vs. Commissioner of Internal Revenue* (*Philippine Journalists* case),[64] the Supreme Court held as follows, to wit:

> "The appellate jurisdiction of the CTA is not limited to cases which involve decisions of the Commissioner of Internal Revenue on matters relating to assessments or refunds. The second part of the provision covers other cases that arise out of the NIRC or related laws administered by the Bureau of Internal Revenue. The wording of the provision is clear and simple. **It gives the CTA the jurisdiction to determine if the warrant of distraint and levy issued by the BIR is valid** and to rule if the Waiver of Statute of Limitations was validly effected." *(Emphasis supplied)*

Clearly, the validity of a WDL is an issue that falls under "other matters arising from the NIRC" that is within the

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CERTAIN SECTIONS OF REPUBLIC ACT NO. 1125, AS AMENDED, OTHERWISE KNOWN AS THE LAW CREATING THE COURT OF TAX APPEALS, AND FOR OTHER PURPOSES.

[62] Section 3, 1997 NIRC, as amended.

[63] *Commissioner of Internal Revenue vs. Hambrecht & Quist Philippines, Inc.*, G.R. No. 169225, November 17, 2010.

[64] G.R. No. 162852, December 16, 2004.

jurisdiction of this Court to decide upon. Considering that in the present Petition for Review, what is being primarily assailed is the WDL No. 2019-00005 dated January 30, 2019[65] issued by respondent, the same can then be taken cognizance by this Court.

In instances when respondent, without categorically deciding the taxpayer's protest or request for reconsideration or reinvestigation, proceeds with distraint and levy or institutes an action for collection in the ordinary courts, the Supreme Court has considered this an implied denial,[66] appealable to this Court within thirty (30) days from the date that it was notified of the warrant or collection suit.[67]

Relative thereto, Section 11 of RA No. 1125, as amended by RA No. 9282, states, in part, as follows:

> "SEC. 11. *Who May Appeal; Mode of Appeal; Effect of Appeal.* – **Any party adversely affected by a decision, ruling** or inaction of the Commissioner of Internal Revenue...**may file an appeal with the CTA within thirty (30) days after the receipt of such decision or ruling** or after the expiration of the period fixed by law for action as referred to in Section 7(a)(2) herein.
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> xxx xxx xxx." *(Emphases supplied)*

Thus, petitioner had thirty (30) days from receipt of the said WDL No. 2019-00005 dated January 30, 2019 on January 31, 2019[68] or until March 4, 2019,[69] within which to file its appeal before this Court. Correspondingly, the filing of the present Petition for Review on February 1, 2019[70] was timely made.

Based on the foregoing jurisprudence, it is clear that a collection letter, having the character of finality, may be treated as the CIR's final decision, which, in turn, may already be appealed to this Court. As such, the argument of petitioner that

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[65] Exhibit "R-31", BIR Records (Folder 4 of 4), p. 35.
[66] *Commissioner of Internal Revenue vs. Algue, Inc.*, G.R. No. L-28896, February 17, 1988, 241 Phil. 829 (1988) [Per J. Cruz, First Division].
[67] *Commissioner of Internal Revenue vs. South Entertainment Gallery, Inc.*, G.R. No. 225809, March 17, 2021.
[68] Pars. 3 and 16, *Petition for Review*, Docket – Vol. I, pp. 12 and 15, respectively, vis-à-vis Par. 1, *Answer*, Docket – Vol. I, p. 245.
[69] The 30th day fell on March 2, 2019, a Saturday. The next working day would be March 4, 2019, a Monday.
[70] Docket – Vol. I, pp. 12 to 23.

the non-issuance of the FDDA prior to the release of WDL No. 2019-00005 dated January 30, 2019 renders the latter premature and void, must fail.

It is worthy to emphasize that the aforementioned collection letter may fall under the category of "other matters" pursuant to the earlier quoted *Philippine Journalists* case, which, as shown, categorically ruled that this Court's jurisdiction also includes the power "to determine if the warrant of distraint and levy issued by the BIR is valid."

We shall now proceed to determine the other issues raised by the parties.

The LOAs, PANs, and FLDs, were duly served to petitioner.

Section 228 of the 1997 NIRC, as amended, provides for the right of the taxpayer to procedural due process in the issuance of a deficiency tax assessment, to wit:

> "SEC. 228. *Protesting of Assessment.* — When the Commissioner or his duly authorized representative finds that proper taxes should be assessed, he shall first notify the taxpayer of his findings: xxx
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> xxx xxx xxx
>
> **The taxpayers shall be informed in writing of the law and the facts on which the assessment is made; otherwise, the assessment shall be void.**
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> xxx xxx xxx." *(Emphasis supplied)*

The requirement that the taxpayer must be informed of the factual and legal bases of the assessment is mandatory. It cannot be presumed. As a requirement of due process, this rule allows the taxpayer to make an effective protest.[71] To be sure, the requirement set by law to state in writing the factual and legal bases for the assessment is not a hollow exhortation. The

[71] *Commissioner of Internal Revenue vs. Spouses Remigio P. Magaan and Leticia L. Magaan*, G.R. No. 232663, May 3, 2021. *om*

law imposes a substantive, not merely a formal, requirement.[72] Furthermore, it must be emphasized that failure to comply with Section 228 of the 1997 NIRC, as amended, does not only render the assessment void, but also finds no validation in any provision of the Tax Code.[73]

To implement the above-quoted Section 228 of the 1997 NIRC, as amended, Section 3 of Revenue Regulations (RR) No. 12-99,[74] as amended by RR No. 18-2013,[75] provides, in part, as follows:

> "SECTION 3. ***Due Process Requirement in the Issuance of a Deficiency Tax Assessment. –***
>
> 3.1 Mode of procedure in the issuance of a deficiency tax assessment:
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> 3.1.1 *Preliminary Assessment Notice (PAN).* – If after review and evaluation by the Commissioner or his duly authorized representative, as the case may be, it is determined that there exists sufficient basis to assess the taxpayer a Preliminary Assessment Notice (PAN) for the proposed assessment. It shall show in detail the facts and the law, rules and regulations, or jurisprudence on which the proposed assessment is based (see illustration in ANNEX 'A' hereof).
>
> xxx xxx xxx
>
> 3.1.3 *Formal Letter of Demand and Final Assessment Notice (FLD/FAN).* – The Formal Letter of Demand and Final Assessment Notice (FLD/FAN) shall be issued by the Commissioner or his duly authorized representative. **The FLD/FAN calling for payment of the taxpayer's deficiency tax or taxes shall state the facts, the law, rules and regulations, or jurisprudence on which the assessment is based, *otherwise, the assessment shall be void*** (see illustration in ANNEX 'B' hereof).
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> xxx xxx xxx

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[72] *Commissioner of Internal Revenue vs. Unioil Corporation*, G.R. No. 204405, August 4, 2021.

[73] *Id.*, citing *Commissioner of Internal Revenue vs. Reyes*, G.R. Nos. 159694 and 163581, January 27, 2006, 516 Phil. 176, 189 (2006).

[74] SUBJECT: Implementing the Provisions of the National Internal Revenue Code of 1997 Governing the Rules on Assessment of National Internal Revenue Taxes, Civil Penalties and Interest and the Extra-Judicial Settlement of a Taxpayers Criminal Violation of the Code Through Payment of a Suggested Compromise Penalty.

[75] SUBJECT: Amending Certain Sections of Revenue Regulations No. 12-99 Relative to the Due Process Requirement in the Issuance of a Deficiency Tax Assessment. *gm*

> 3.1.5 *Final Decision on a Disputed Assessment (FDDA).* – **The decision of** the Commissioner or **his duly authorized representative <u>shall state the (i) facts, the applicable law</u>, rules and regulations, or jurisprudence on which such decision is based, <u>*otherwise, the decision shall be void*</u>** (see illustration in ANNEX 'C' hereof), and (ii) that the same is his final decision." *(Emphases and underscoring added)*

The foregoing provisions prescribe, as part of due process in the issuance of tax assessments, that the PAN, FLD/FAN and FDDA must, respectively, state, among others, the facts and the law on which the assessment is based; otherwise, the FLD/FAN and/or FDDA shall be void.

Records evidently show that respondent duly notified petitioner of the subject assessment notices as shown by the following: that petitioners received LOA No. 015-2014-00000007 for TY 2011, LOA No. 015-2014-00000008 for TY 2012, and LOA No. 015-2014-00000009 for TY 2013 on June 13, 2014;[76] that petitioner received the PAN dated April 6, 2015[77] for TY 2013 on April 14, 2015, while the PAN dated February 16, 2015[78] for TY 2011 and PAN dated April 10, 2015[79] for TY 2012 were both received by petitioner on April 22, 2015; and, that petitioner received respondent's FLD dated June 22, 2015[80] for TY 2011, FLD dated June 22, 2015[81] for TY 2012, and FLD dated June 22, 2015[82] for TY 2013 on June 25, 2015.

Respondent's right to assess petitioner of deficiency VAT for the four (4) quarters of TY 2011, and 1st quarter of 2012, is barred by prescription.

The period for the filing of quarterly VAT returns is provided in Section 114 (A) of the 1997 NIRC, as amended, which reads:

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[76] Par. 3, Joint Stipulation of Facts, JSFI, Docket – Vol. I, p. 382; Exhibits "P-1" and "R-1", BIR Record (Folder 1 of 4), p. 2; Exhibits "P-2" and "R-19", BIR Records (Folder 3 of 4), p. 345; Exhibits "P-3" and "P-10", BIR Records (Folder 2 of 4), p. 118.
[77] Exhibits "R-15" to "R-15-A" and "P-4", BIR Records (Folder 2 of 4), pp. 580 to 583.
[78] Exhibits "R-6" to "R-6-A", BIR Records (Folder 1 of 4), pp. 265 to 269.
[79] Exhibits "R-24" to "R-24-A", BIR Records (Folder 3 of 4), pp. 475 to 478.
[80] Exhibits "R-7" to "R-7-B", BIR Records (Folder 1 of 4), pp. 272 to 279.
[81] Exhibits "R-25" to "R-25-B", BIR Record (Folder 3 of 4), pp. 481 to 494.
[82] Exhibits "R-16" to "R-16-B", BIR Records (Folder 2 of 4), pp. 594 to 599.

> *"SEC. 114. Return and Payment of Value-Added Tax. –*
>
> (A) *In General.* — **Every person liable to pay the value-added tax imposed under this Title shall file a quarterly return of the amount of his gross sales or receipts within twenty-five (25) days following the close of each taxable quarter prescribed for each taxpayer**: *Provided, however,* That VAT-registered persons shall pay the value-added tax on a monthly basis." *(Emphasis supplied)*

In relation thereto, Section 203 of the same Code provides:

> "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 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**." *(Emphasis supplied)*

Petitioner filed its Quarterly VAT Returns for the four (4) quarters of TY 2011 and the 1st quarter of TY 2012 on the last day prescribed by law for the filing of such returns, as shown hereafter, *vis-à-vis* the date when the FLD was received:

VAT	Quarterly Return Filed/Due	End of three (3) years	FLD Received[83]
TY 2011			
1st Quarter	25 April 2011[84]	25 April 2014	25 June 2015
2nd Quarter	25 July 2011[85]	25 July 2014	25 June 2015
3rd Quarter	25 October 2011[86]	25 October 2014	25 June 2015
4th Quarter	25 January 2012[87]	25 January 2015	25 June 2015
TY 2012			
1st Quarter	25 April 2012[88]	25 April 2015	25 June 2015

Based on the above table, the deficiency VAT assessments for the four (4) quarters of TY 2011 and 1st quarter of 2012 were issued beyond the three (3)-year period as mandated by Section

[83] Exhibit "R-7", BIR Records (Folder 1 of 4), pp. 278 to 279; Exhibit "R-25", BIR Records (Folder 3 of 4), pp. 493 to 494.
[84] BIR Records (Folder 1 of 4), p. 124.
[85] BIR Records (Folder 1 of 4), p.116.
[86] BIR Records (Folder 1 of 4), p.108.
[87] BIR Records (Folder 1 of 4), p.100.
[88] BIR Records (Folder 3 of 4), p. 114.

203 of the 1997 NIRC, as amended. Thus, respondent is barred by prescription from assessing petitioner of deficiency VAT for the said periods.

Respondent's right to assess petitioner of the unpaid annual registration fee for TY 2011 has not yet prescribed.

The payment of the annual registration fee is required under Section 236 of the 1997 NIRC, as amended, which states:

> "SEC. 236. *Registration Requirements.—*
>
> xxx
>
> (B) *Annual Registration Fee.* — **An annual registration fee in the amount of Five hundred pesos (₱500) for every separate or distinct establishment or place of business**, including facility types where sales transactions occur, **shall be paid upon registration and every year thereafter on or before the last day of January**: *Provided, however,* That cooperatives, individuals earning purely compensation income, whether locally or abroad, and overseas workers are not liable to the registration fee herein imposed." *(Emphasis supplied)*

It is clear from the foregoing that the annual registration fee in the amount of five hundred pesos (₱500.00) for every separate or distinct establishment or place of business should be paid by the establishment on or before the last day of January.

Since the Annual Registration Fee is not considered a tax, the three (3)-year period to assess the taxpayer under the afore-quoted Section 203 of the 1997 NIRC, as amended, does not apply. Instead, Article 1149 of the New Civil Code prescribing a five (5)-year prescriptive period shall be adopted in determining the statute of limitations to assess and collect said fees. We quote Article 1149 of the New Civil Code as follows:

> "Article 1149. All other actions whose periods are not fixed in this Code or in other laws must be brought within five (5) years from the time the right of action accrues."

In this case, petitioner's last day to pay its annual registration fee for its establishments or places of business for the TY 2011 was on January 31, 2011, hence, the FLD, which was issued on June 22, 2015 and received by petitioner on June 25, 2015, was still within the five (5)-year period to assess and collect.

Respondent timely assessed petitioner of deficiency IAET.

As to the IAET assessment, Section 6 of RR No. 2-2001[89] states:

> "SECTION 6. *Period for Payment of Dividend/ Payment of IAET.* — **The dividends must be declared and paid or issued not later than one year following the close of the taxable year, otherwise, the IAET, if any, should be paid within fifteen (15) days thereafter.**" *(Emphasis supplied)*

Based on the foregoing, petitioner's last day to declare and pay dividends from its income for the TY 2011 was on December 31, 2012. Thus, fifteen (15) days therefrom or until January 15, 2013, the IAET should have been paid. Thus, counting three (3) years from January 15, 2013, the period to assess petitioner of deficiency IAET is until January 15, 2016. Consequently, the FLD issued on June 22, 2015 and received by petitioner on June 25, 2015 was issued within the three (3)-year period.

Having settled the foregoing matters, the Court shall now ascertain the propriety of the deficiency tax assessments for TYs 2011 to 2013.

<u>For TY 2011</u>

Petitioner is liable for deficiency income tax for TY 2011.

Per the pertinent FLD,[90] respondent found petitioner liable for deficiency income tax, inclusive of penalties, as follows:

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[89] SUBJECT: Implementing the Provision on Improperly Accumulated Earnings Tax Under Section 29 of the Tax Code of 1997.
[90] Exhibit "R-7", BIR Records (Folder 1 of 4), p. 279.

Taxable Income per Return		₱4,107,253.41
Adjustments per Audit:		
Disallowed Unsupported Expenses	7,622,438.43	
Undeclared Expenses	398,878.25	
Unsupported Purchases	60,015,022.15	68,036,338.83
Taxable Income per Audit		₱ 72,143,592.24
Income Tax Due		₱ 21,643,077.67
Less: Tax Paid per return		983,306.29
Deficiency Income Tax		₱ 20,659,771.38
Add: 50% Surcharge	₱10,329,885.69	
20% Interest from 04-15-2012 to 06-22-2015	13,348,507.84	23,678,393.53
Total Deficiency Income Tax		**₱ 44,338,164.91**

The adjustments above are broken down in the Details of Discrepancies[91] attached to the FLD, and shall be addressed hereafter.

Disallowed Unsupported Expenses

Respondent's examiner found that the following expenses or deductions claimed by petitioner are unsupported:[92]

Taxes & Licenses	₱ 139,883.62
Communication, Light and Water	238,314.12
Fuel & Oil	1,258,648.75
Repairs and Maintenance	130,360.00
LTO Registration	196,375.18
Insurance Expense	1,903.65
Retainer's Fee	44,375.00
Interest Expense	3,410,291.65
Representation Expense	12,350.00
Miscellaneous Expense	12,824.26
Donation/Contribution	30,250.00
Rental Expense	120,000.00
Legal and Auditing Fees	60,372.20
Supplies Expense	30,265.00
Advertisement	14,650.00
Salaries & Wages - 50%	1,560,325.00
Depreciation Expense	361,250.00
Total Disallowed Unsupported Expenses	**₱7,622,438.43**

Upon scrutiny of the records, the Court notes that respondent's assessment of income tax was based on the

[91] Exhibit "R-7-A", BIR Records (Folder 1 of 4), pp. 276 to 277.
[92] Exhibit "R-7-A", BIR Records (Folder 1 of 4), p. 277. *om*

Statement of Comprehensive Income submitted by petitioner when it filed its original Income Tax Return (ITR) for the year 2011, thus:

	Expenses per Financial Statements (FS)-Original Filing[93]	**Supported Expenses**[94]	**Unsupported Expenses Per BIR Audit**
Salaries & Wages	₱ 3,120,650.00	₱ 1,560,325.00[95]	₱ 1,560,325.00
Taxes & Licenses	139,883.62	-	139,883.62
Communication, Light and Water	340,915.25	102,601.13	238,314.12
Fuel & Oil	1,263,205.75	4,557.00	1,258,648.75
Repairs and Maintenance	170,320.00	39,960.00[96]	130,360.00
LTO Registration	196,375.18	-	196,375.18
Insurance Expense	46,377.25	44,473.60	1,903.65
Retainer's Fee	44,375.00	-	44,375.00
Interest Expense	3,410,291.65	-	3,410,291.65
Representation Expense	12,350.00	-	12,350.00
Miscellaneous Expense	65,367.00	52,542.74	12,824.26
Donation/Contribution	30,250.00	-	30,250.00
Rental Expense	120,000.00	-	120,000.00
Legal and Auditing Fees	60,372.20	-	60,372.20
Supplies Expense	30,265.00	-	30,265.00
Advertisement	16,750.00	2,100.00	14,650.00
Depreciation Expense	361,250.00	-	361,250.00
TOTALS	**₱9,428,997.90**	**₱1,806,559.47**	**₱7,622,438.43**

The Court likewise notes that petitioner reported different amounts of the subject expenses in its amended financial statements. Consequently, the amounts of unsupported expenses should be adjusted as follows:

	Expenses per Amended FS[97]	**Supported Expenses**[98]	**Adjusted Unsupported Expenses per BIR Audit**
Salaries & Wages	₱ 3,090,000.00	₱ 1,545,000.00[99]	₱ 1,545,000.00
Taxes & Licenses	187,008.40	-	187,008.40

[93] BIR Records (Folder 1 of 4), p. 139.
[94] BIR Records (Folder 1 of 4), pp. 165 to 166.
[95] Respondent's examiner just multiplied the salaries & wages expense per FS by 50%.
[96] BIR Records (Folder 1 of 4), pp. 160 and 166. [₱23,814.00 + ₱16,146.00]
[97] Exhibit "P-22", Annexes 14 and 17-17.
[98] BIR Records (Folder 1 of 4), pp. 165 to 166.
[99] Respondent's examiner just multiplied the salaries & wages expense per FS by 50%. an

Communication, Light & Water	378,522.25	102,601.13	275,921.12
Fuel & Oil	1,112,619.31	4,557.00	1,108,062.31
Repairs and Maintenance	63,252.36	39,960.00[100]	23,292.36
LTO Registration	7,695.63	-	7,695.63
Insurance Expense	6,252.33	44,473.60	
Retainer's Fee	-	-	-
Interest Expense	3,243,677.05	-	3,243,677.05
Representation Expense	13,381.42	-	13,381.42
Miscellaneous Expense	442,094.94	52,542.74	389,552.20
Donation/Contribution	5,000.00	-	5,000.00
Rental Expense	120,000.00	-	120,000.00
Legal and Auditing Fees	-	-	-
Supplies Expense	30,265.00	-	30,265.00
Advertisement	-	2,100.00	
Depreciation Expense	432,893.43	-	432,893.43
TOTALS	**₱ 9,132,662.12**	**₱1,791,234.47**	**₱7,381,748.92**

On the other hand, the ICPA found that only the amount of ₱152,308.00 was supported by estimate papers, official receipts, receipts, sales invoices, VAT charge invoices, and VAT sales invoices.[101]

Since petitioner failed to substantially refute respondent's assessment, this Court has no recourse but to uphold the disallowance of unsupported expenses in the modified amount of ₱7,381,748.92.

Undeclared Expenses deemed undeclared income

Respondent's examiner found that there was a discrepancy in the amounts declared in the following expenses vis-à-vis expenses declared in petitioner's financial statements, *viz.*:

PhilHealth	₱103,925.00[102]
SSS	325,164.00[103]

[100] BIR Records, Folder 1 of 4, pp. 160 and 166. [₱23,814.00 + ₱16,146.00].
[101] Exhibit "P-22", Docket – Vol. II, p. 612.
[102] BIR Records (Folder 1 of 4), p. 169.
[103] BIR Records (Folder 1 of 4), p. 168.

HDMF	106,110.00[104]
Total	₱ 535,199.00
Less: Declared per Financial Statements-Original Filing	136,320.75[105]
Total undeclared expenses	**₱398,878.25**[106]

Consequently, respondent's examiner considered the undeclared expenses in the amount of ₱398,878.25 as undeclared income subject to income tax.

However, the Court notes that in petitioner's amended financial statements, the aggregate amount of petitioner's contributions to SSS, PhilHealth, and HDMF (Pag-IBIG) was ₱141,500.50. [107] Thus, the computation thereon should be modified in this wise:

Total SSS/PhilHealth/HDMF	₱ 535,199.00
Less: Declared per amended Financial Statements	141,500.50
Total adjusted undeclared expenses	**₱393,698.50**

Notwithstanding the foregoing, the Court finds the above item of assessment bereft of merit.

Notably, an "unaccounted expense" should not be automatically treated as income, to which income tax should be imposed. Jurisprudence defines income as an amount of money coming to a person within a specified time, whether as payment for services, interest, or profit from investment. It means cash or its equivalent. It is gain derived and severed from capital, from labor or from both combined. Thus, the determining factor for the imposition of income tax is whether there was any gain or profit derived from a certain transaction. [108]

Unlike income, the taxpayer does not gain any profit whenever the latter incurs expenses and, in fact, spends money to pay for said expenses.

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[104] BIR Records (Folder 1 of 4), p. 167.
[105] BIR Records (Folder 1 of 4), p. 139.
[106] Exhibit "R-7-A", BIR Records (Folder 1 of 4), p. 277.
[107] Exhibit "P-22", Annexes 14 and 17-17.
[108] *Commissioner of Internal Revenue vs. Court of Appeals, et al.,* G.R. No. 108576, January 20, 1999.

It bears stressing that for income tax purposes, a taxpayer is free to deduct from its gross income a lesser amount, or not to claim any deduction at all. What is prohibited by the income tax law is to claim a deduction beyond the amount authorized therein.[109] Thus, even when a taxpayer has not claimed expenses or declared a lesser amount thereof in the ITR, such action is allowed, and shall not necessarily result in the imposition of income tax on the undeclared deduction or unaccounted expenses.

In this case, there being no gain or profit derived from such unaccounted expenses, the income tax imposition thereon should be cancelled.

Unsupported Purchases

Respondent likewise found petitioner's purchases amounting to ₱60,015,022.15 as unsupported, *viz.*:[110]

Purchases per Income Statement	₱100,101,037.05
Purchases per source documents	40,086,014.90
Total unsupported purchases	**₱60,015,022.15**

Respondent based its computation on petitioner's financial statements, attached to its annual ITR, originally filed on April 13, 2012. In the said ITR, the declared purchases of petitioner amounted to ₱100,101,037.05.[111] However, its reported purchases in its amended statement of comprehensive income amounted to ₱97,303,359.68.[112] Of the said amounts, the ICPA was only able to examine the amount of ₱19,159,117.42,[113] which is lower than ₱40,086,014.90 found by respondent's examiner to have been duly supported with source documents.[114] Moreover, of the amount examined by the ICPA, only ₱2,560,164.75 was found to have complied with the requirements of deductibility.[115] Hence, the Court is constrained to uphold respondent's assessment thereon with the following modification:

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[109] *Commissioner of Internal Revenue vs. Phoenix Assurance Co. Ltd., et seq.*, G.R. Nos. L-19727 and L-19903, May 20, 1965.
[110] Exhibit "R-7-A", BIR Records (Folder 1 of 4), p. 276 and BIR Records (Folder 1 of 4), p. 250.
[111] BIR Records (Folder 1 of 4), p. 139.
[112] Exhibit "P-22", Annexes 14 and 17-17.
[113] Exhibit "P-22", Docket – Vol. II, pp. 610 to 611.
[114] Exhibit "R-7-A", BIR Records (Folder 1 of 4), p. 276.
[115] Exhibit "P-22", Docket – Vol. II, p. 645.

Purchases per Income Statement	₱ 97,303,359.68
Purchases per source documents	40,086,014.90
Total unsupported purchases	**₱57,217,344.78**

In computing the deficiency income tax, respondent deducted the amount of ₱983,306.29 as "Tax Paid per return", [116] which consists of amounts picked up from the originally-filed ITR and the amended ITR:

Amounts from originally-filed ITR:		
Income tax paid from previous quarters[117]	₱ 2,635.00	
Income Tax paid[118]	92,465.00	₱ 95,100.00
Other credits (Additional Payment)[119]		250,000.00
Aggregate Income Tax due per amended ITR[120]		638,206.29
Total Tax Paid per Return		**₱ 983,306.29**

However, a scrutiny of the amended ITR of petitioner shows the following:[121]

Income tax due	₱ 1,232,176.00
Tax Credits/Payments:	
Income tax paid from previous quarters	₱ 58,135.00
Creditable Tax Withheld	193,369.71
Income Tax paid in Return previously filed, if this is an amended return	92,465.00
Other credits (Additional Payment)	250,000.00
Total Tax Credits/Payments	₱ 593,969.71
Tax Payable	**₱ 638,206.29**

It must be noted that respondent did not consider the amended income tax paid from previous quarters and the creditable tax withheld of petitioner.

Examination of the BIR Records show that the Taxpayer Ledger Inquiry for income tax in the BIR Taxpayer Accounting System reports the following payments from petitioner for the TY 2011:[122]

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116 Exhibit "R-7", BIR Records (Folder 1 of 4), p. 279.
117 BIR Records (Folder 1 of 4), Line 33B, p. 136.
118 BIR Records (Folder 1 of 4), Line 34B, pp. 136 and 144.
119 Exhibit "R-5", BIR Records (Folder 1 of 4), Item No. 3, p. 254.
120 BIR Records (Folder 1 of 4), p. 150.
121 Exhibit "P-22", Lines 28 to 34 of Annex 11-2.
122 BIR Records (Folder 1 of 4), p. 234.

Date	Transaction Type	Amount
April 13, 2012	PYT	₱ 92,465.00
April 16, 2012	WHT	213,061.00
February 11, 2014	PYT	871,457.50[123]
November 29, 2013	PYT	250,000.00
	Total	**₱1,426,983.50**

From the foregoing, respondent's system - recorded payments for income tax from petitioner were in the aggregate amount of ₱1,193,732.21:

Total payments per BIR Taxpayer Accounting System	₱1,426,983.50
Less: Interest paid per amended ITR[124]	233,251.29
Total Tax Paid per Return	**₱1,193,732.21**

In sum, petitioner is liable for deficiency income tax for TY 2011 in the adjusted amount of ₱19,418,171.92, computed thus:

Taxable Income per Return		₱ 4,107,253.41
Adjustments:		
Disallowed Unsupported Expenses	₱7,381,748.92	
Unsupported Purchases	57,217,344.78	64,599,093.70
Taxable Income per Audit		₱ 68,706,347.11
Income Tax Due (30%)		₱ 20,611,904.13
Less: Tax Paid per return		1,193,732.21
Deficiency Income Tax		**₱ 19,418,171.92**

Petitioner is liable for IAET for TY 2011.

Claiming that petitioner retained more than the reasonable needs of the business, respondent subjected petitioner to IAET, to wit:[125]

Taxable Income per Audit		₱ 72,143,592.24
Add: Retained Earnings from prior years		4,599,133.22
Total		₱ 76,742,725.46
Less: Income Tax paid	₱ 733,306.29	

[123] The amount consists of Income tax payable of ₱638,206.29 and Interest of ₱233,251.29. Only the amount ₱638,206.29 is the payment for income tax.
[124] Exhibit "P-22", Line 36B, Annex 11-2.
[125] Exhibit "R-7", BIR Records (Folder 1 of 4), p. 278. Gm

Amount to be retained (100% Paid-up Capital)	125,000.00	858,306.29
Improperly Accumulated Earnings		₱ 75,884,419.17
Multiply by IAET Rate		10%
IAET		₱ 7,588,441.92
Add: 50% Surcharge	₱3,794,220.96	
20% Interest from 01-25-2012 to 06-22-2015	5,286,614.54	9,080,835.50
Total Deficiency IAET		**₱16,669,277.42**

Section 29 (E) of the 1997 NIRC, as amended, defines "reasonable needs of the business" as one that "includes the reasonably anticipated need of the business." We quote Sections 2 and 3 of RR No. 2-2001 [126] to ascertain what constitutes as "reasonable needs of the business":

> "SEC. 3. *Determination of Reasonable Needs of the Business.* — Accumulation of earnings or profits (including undistributed earnings or profits of prior years) is unreasonable if it is not necessary for the purpose of the business, considering all the circumstances of the case. To determine the 'reasonable needs' of the business in order to justify an accumulation of earnings, these Regulations hereby adhere to the so-called **'Immediacy Test'** under American jurisprudence as adopted in this jurisdiction. **Accordingly, the term *'reasonable needs of the business'* are hereby construed to mean the immediate needs of the business, including reasonably anticipated needs. In either case, the corporation should be able to prove an immediate need for the accumulation of the earnings and profits, or the direct correlation of anticipated needs to such accumulation of profits.** Otherwise, such accumulation would be deemed to be not for the reasonable needs of the business, and the penalty tax would apply.
>
> xxx xxx xxx
>
> For purpose of these Regulations, the following constitute accumulation of earnings for the reasonable needs of the business:
>
> a. Allowance for the increase in the accumulation of earnings up to 100% of the paid-up capital of the corporation as of Balance Sheet date, inclusive of accumulations taken from other years;
>
> b. **Earnings reserved for definite corporate expansion projects or programs requiring considerable capital expenditure as approved by the Board of Directors or equivalent body**;

[126] SUBJECT: Implementing the Provision on Improperly Accumulated Earnings Tax Under Section 29 of the Tax Code of 1997.

c. Earnings reserved for building, plants or equipment acquisition as approved by the Board of Directors or equivalent body;

d. Earnings reserved for compliance with any loan covenant or pre-existing obligation established under a legitimate business agreement;

e. Earnings required by law or applicable regulations to be retained by the corporation or in respect of which there is legal prohibition against its distribution;

f. In the case of subsidiaries of foreign corporations in the Philippines, all undistributed earnings intended or reserved for investments within the Philippines as can be proven by corporate records and/or relevant documentary evidence." *(Emphases supplied).*

In this case, petitioner alleges that the reasonable needs of its business fall under Section 3 (b) of RR No. 2-2001. To show that retained earnings were appropriated by petitioner, it submitted a copy of Secretary's Certificate of Board Resolution No. 3 dated February 7, 2014, showing that it appropriated the amount of ₱7,400,000.00 for plant expansion.[127]

Upon scrutiny of the records, the Court notes that petitioner's amended Statement of Comprehensive Income for the year 2011 shows net income after provision for income tax in the amount of ₱2,875,077.38. [128] Corollary thereto, its amended Statement of Changes in Equity contains the following details:[129]

	Share Capital	**Cumulative Unappropriated**	**Earnings Appropriated**	**Total Equity**
Balance at December 31, 2009	₱125,000.00	₱ 66,911.97	₱3,400,000.00	₱3,591,911.97
Net Profit/(Loss) for the year		1,132,221.25		1,132,221.25
Appropriation from retained earnings		(1,130,000.00)	1,130,000.00	-
Balance at December 31, 2010	₱125,000.00	₱ 69,133.22	₱4,530,000.00	₱4,724,133.22
Net Profit/(Loss) for the year		2,875,077.41		2,875,077.41
Appropriation from retained earnings		(2,870,000.00)	2,870,000.00	-
Balance at December 31, 2011	**₱125,000.00**	**₱ 74,210.63**	**₱7,400,000.00**	**₱7,599,210.63**

[127] Exhibit "P-22", Annex 25.
[128] Exhibit "P-22", Annex 14.
[129] Exhibit "P-22", Annex 15.

It can be inferred from petitioner's amended financial statements that it has been appropriating its earnings since TY 2009. Thus, when the Board appropriated ₱7,400,000.00 for plant expansion in the year 2011, only the amount of ₱2,870,000.00 was actually appropriated, as the amount of ₱4,530,000.00 has been appropriated in 2010.[130] However, petitioner's comparative Statement of Financial Position for the years 2010 and 2011,[131] particularly Note 8 of the Notes to the Financial Statements, shows that its Property, Plant and Equipment account has no additions.[132] This indicates that the appropriated amount of ₱4,530,000.00 in the year 2010 was not used for plant expansion. Further, even the petitioner's amended comparative Statement of Financial Position for the years 2011 and 2012[133] likewise shows that the amount of ₱2,870,000.00 remained unused for plant expansion for the year 2011, and that the only addition to petitioner's Property, Plant and Equipment account was its Trucks and Vehicles in the amount of ₱610,000.00.

It equally bears noting that the Board Resolution appropriated the amount of ₱7,400,000.00 for plant expansion only on February 7, 2014, or more than two (2) years after the close of the TY 2011.

In view of the foregoing, it is evident that the delay in the utilization of petitioner's appropriated earnings for its supposed plant expansion only proves that there was no immediate need for such appropriation or accumulation of its earnings. Petitioner, therefore, failed to establish, by clear and preponderance of evidence, the definite plan of expansion as well as the actions taken by the company to consummate the same. Thus, the Court finds petitioner liable for IAET.

However, this Court finds it proper to modify the computation of the IAET by starting with petitioner's taxable income for the year 2011, and not with the taxable income as found by respondent's audit, as petitioner cannot be expected to appropriate or declare as dividends within the prescribed period the income for the year 2011 that was found by respondent's examiner in the year 2015.

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[130] Exhibit "P-22", Annex 15.
[131] Exhibit "P-22", Annex 13.
[132] Exhibit "P-22", Annexes 17-15.
[133] BIR Records (Folder 3 of 4), p. 310.

Moreover, Section 5 of RR No. 2-2001, the regulation implementing Section 29 of the 1997 NIRC, as amended, specifically mentions that the computation of IAET starts with the taxable income, thus:

> "SEC. 5. *Tax Base of Improperly Accumulated earnings Tax.* — For corporations found subject to the tax, the *'Improperly Accumulated Taxable Income'* for a particular year is first determined by adding to **that year's taxable income** the following:
>
> a. income exempt from tax;
> b. income excluded from gross income;
> c. income subject to final tax; and
> d. the amount of net operating loss carry-over (NOLCO) deducted.
>
> The taxable income as thus determined shall be reduced by the sum of:
>
> a. income tax paid/payable for the taxable year;
> b. dividends actually or constructively paid/issued from the applicable year's taxable income;
> c. amount reserved for the reasonable needs of the business as defined in these Regulations emanating from the covered year's taxable income.
>
> The resulting *'Improperly Accumulated Taxable Income'* is thereby multiplied by 10% to get the Improperly Accumulated Earnings Tax (IAET)." *(Emphasis supplied)*

This is reinforced by Revenue Memorandum Circular (RMC) No. 035-11[134] which spells out clearly how the Improperly Accumulated Taxable Income (IATI) should be computed, thus:

> "III. *Computation of Improperly Accumulated Taxable Income*
>
> By way of illustration, Improperly Accumulated Taxable Income (IATI) is computed as follows:

Taxable Income for the year (e.g., 2010)		Pxxxx
Add:		
(a) Income subjected to Final Tax	Pxxx	
(b) NOLCO	xxx	
(c) Income exempt from tax	xxx	
(d) Income excluded from gross income	xxx	xxxx
		Pxxxx

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134 SUBJECT: Clarification of Issues Concerning the Imposition of Improperly Accumulated Earnings Tax Pursuant to Section 29 of the Tax Code of 1997, in Relation to Revenue Regulations No. 2-2001.

Less:		
Income Tax paid	Pxxx	
Dividends declared/paid	xxx	xxxx
Total		Pxxxx
Add: Retained Earnings from prior years		
Accumulated Earnings as of December 31, 2010	xxxx	
Less: Amount that may be Retained (100% of Paid-Up Capital as of December 31, 2010)		xxxx
IATI		Pxxxx

The resulting 'Improperly Accumulated Taxable Income' is thereby multiplied by 10% to arrive at the Improperly Accumulated Earnings Tax (IAET)." (Emphasis supplied)

Thus, it is clear from the foregoing that the computation of IAET starts with the taxpayer's taxable income, and **not** with the taxable income per audit. Consequently, petitioner's IAET should be ₱738,765.44, computed as follows:

Taxable income per amended financial statements and ITR[135]		₱4,107,253.41
Add: Retained Earnings from prior years[136]		4,599,133.22
Total		₱8,706,386.63
Less: Income tax paid	₱1,193,732.21	
Amount to be retained (100% Paid-up Capital)	125,000.00	1,318,732.21
Improperly Accumulated Earnings		₱7,387,654.42
Multiply by IAE Tax rate		10%
Improperly Accumulated Earnings Tax		**₱738,765.44**

In fine, petitioner's deficiency tax liabilities for the TY 2011, excluding surcharges and penalties, are as follows:

	Tax Deficiency/Liability
Income tax	₱ 19,418,171.92
Improperly Accumulated Earnings Tax	738,765.44
Total	**₱ 20,156,937.36**

135 Exhibit "P-22", Annexes 11-1, 11-2 and 14.
136 Exhibit "P-22", Annex 15. [₱69,133.22 + ₱4,530,000.00]

<u>For TY 2012</u>

Petitioner is liable for deficiency income tax for TY 2012.

Respondent found the following deficiency income tax for the TY 2012, including surcharge and penalties:[137]

Taxable Income per Return		₱4,335,018.00
Adjustments per Audit:		
Unsupported Purchases	₱56,968,336.57	
Unsupported Expenses	11,116,597.21	
Undeclared Non-VAT Purchases	377,815.13	
Undeclared Expenses	208,982.80	68,671,731.71
Taxable Income per Audit		₱ 73,006,749.71
Income Tax Due		₱ 21,902,024.91
Less: Tax Paid per return		417,926.36
Deficiency Income Tax		₱ 21,484,098.55
Add: 50% Surcharge	₱10,742,049.28	
20% Interest from 04-15-2013 to 06-22-2015	9,524,617.03	20,266,666.31
Total Deficiency Income Tax		**₱41,750,764.86**

Based on the foregoing, the deficiency income tax arose from the following items of assessment: (1) unsupported purchases; (2) unsupported expenses; (3) undeclared non-VAT purchases; and (4) undeclared expenses.

<u>Unsupported Purchases</u>

Respondent's examiner computed the amount of unsupported purchases in this wise:[138]

Purchases per Income Statement	₱ 99,435,043.97
Purchases per source documents	42,466,707.40
Total unsupported purchases	**₱56,968,336.57**

However, the ICPA stated in his report that he was only able to examine purchases amounting to ₱1,070,883.18, as these were the only purchases duly supported by delivery

[137] Exhibit "R-25", BIR Records (Folder 3 of 4), p. 494.
[138] Exhibit "R-25-A", BIR Records (Folder 3 of 4), p. 492.

receipts and packing lists.[139] Consequently, the Court has no recourse but to uphold said disallowance, for failure on the part of petitioner to disprove the foregoing audit findings with documentary evidence.

Unsupported Expenses

Similarly, respondent found that the following expenses were unsupported and, thus, disallowed the same:[140]

Salaries & Wages - 50% disallowed	₱ 1,608,750.00
Taxes & Licenses	214,353.14
Communication, Light & Water	244,663.13
Fuel & Oil	1,344,327.82
Repairs and Maintenance	67,446.11
LTO Registration	12,285.00
Interest Expense	7,445,440.81
Miscellaneous Expense	174,331.20
Donation/Contribution	5,000.00
Total Disallowed Unsupported Expenses	**₱11,116,597.21**

Per Note 17 of petitioner's Amended *Notes to the Financial Statements*, the subject expense accounts have the following balances as of the end of 2012. However, only the amount of ₱1,885,188.72 is supported per respondent's audit:

	Per Amended Notes to the Financial Statements[141]	**Supported Expenses per Audit**[142]	**Disallowed Unsupported Expenses**
Salaries & Wages	₱ 3,217,500.00	₱1,608,750.00[143]	₱ 1,608,750.00
Taxes & Licenses	214,353.14	-	214,353.14
Communication, Light & Water	375,772.36	131,109.23	244,663.13
Fuel & Oil	1,392,525.36	48,197.54	1,344,327.82
Repairs and Maintenance	105,232.36	37,786.25	67,446.11
LTO Registration	17,985.00	5,700.00	12,285.00
Interest Expense	7,445,440.81	-	7,445,440.81
Miscellaneous Expense	227,976.90	53,645.70	174,331.20
Donation/Contribution	5,000.00	-	5,000.00
Total	**₱13,001,785.93**	**₱1,885,188.72**	**₱11,116,597.21**

139 Exhibit "P-22", Docket – Vol. II, p. 625.
140 Exhibit "R-25-A", BIR Records (Folder 3 of 4), p. 492.
141 BIR Records (Folder 3 of 4), p. 308.
142 BIR Records (Folder 3 of 4), pp. 402 to 410.
143 Respondent's examiner simply multiplied the expense amount by 50%.

Unfortunately, the ICPA found that all of petitioner's claimed expenses for TY 2012 were not duly supported with documentary evidence.[144] Thus, the disallowance thereon should be upheld.

Undeclared Non-VAT Purchases and Expenses

Respondent also found the following undeclared non-VAT purchases and expenses, and deemed the same to be undeclared income:[145]

Undeclared Non Vatable Purchases:	
(₱314,720/83.30)	₱ 377,815.13
Undeclared Expenses deemed Undeclared Income:	
SSS/PhilHealth/HDMF	₱ 179,650.00
Insurance expense	10,296.99
Representation Expense	15,284.17
Supplies Expense	2,951.64
Professional Fee	800.00
Total undeclared expenses	₱ 208,982.80
TOTAL	**₱586,797.93**

As previously discussed, undeclared purchases and expenses deemed undeclared sales do not give rise to any taxable income, thus should be cancelled.

It is noted that in the FLD, respondent's examiner deducted the amount of ₱417,926.36 as "Tax Paid per return" from petitioner's income tax due per audit. Upon examination of the BIR Records, however, the Court finds that total income tax payments for TY 2012 amounts to ₱1,051,447.22, broken down as follows:

BIR Records (Exhibit "R-27"), Folder 3 of 4	**Date**	**Particulars**	**Amount**
pp. 278 & 278-A	April 13, 2012	1st Quarter payment	₱ 4,365.00
pp. 279 & 279-A	August 15, 2012	2nd Quarter payment	5,470.00
pp. 280 & 280-A	November 12, 2012	3rd Quarter payment	6,435.00
pp. 296 to 298	March 15, 2013	Original ITR Filing	52,604.00
pp. 337 to 338	November 29, 2013	Additional payment	250,000.00
pp. 332 to 336	February 13, 2014	Amended ITR Filing	723,070.35
pp. 400 to 401	2012	Supported CWT per audit	9,502.87
		Total	**₱1,051,447.22**

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[144] Exhibit "P-22", Docket – Vol. II, p. 627.
[145] Exhibit "R-25-A", BIR Records (Folder 3 of 4), pp. 491 to 492.

In sum, petitioner is liable for deficiency income tax for TY 2012 in the adjusted amount of ₱20,674,538.31, as computed below:

Taxable income per Return		₱4,335,018.00
Adjustments per Audit:		
Unsupported purchases	₱56,968,336.57	
Unsupported expenses	11,116,597.21	68,084,933.78
Taxable income per Audit		₱ 72,419,951.78
Income Tax Due		₱ 21,725,985.53
Less: Tax Paid per return		1,051,447.22
Deficiency Income Tax		**₱20,674,538.31**

Petitioner is liable for deficiency VAT for TY 2012.

Respondent assessed petitioner with deficiency VAT for TY 2012 as follows:[146]

Undeclared income		₱ 208,982.80
Multiply by VAT Rate		12%
VAT Due on Undeclared Sales		₱ 25,077.94
Add: Disallowed Input Tax on Unsupported Purchases	₱7,045,577.65	
Unsupported Certificate of Tax Credit	1,017.78	7,046,595.43
Total Deficiency VAT		₱ 7,071,673.37
Add: 50% Surcharge	₱3,535,836.68	
20% Interest from 01-25-2013 to 06-22-15	3,449,405.12	6,985,241.80
Total Deficiency VAT		**₱14,056,915.17**

The assessment items will be discussed in sequence. However, as previously discussed, respondent's right to assess petitioner of deficiency VAT for the 1st quarter of 2012 is time-barred. Consequently, the foregoing assessment must be adjusted to take out/cancel the prescribed portion.

<u>*Undeclared income*</u>

It is noted that the undeclared income assessed for deficiency VAT amounting to ₱208,982.80 comes from the income tax deficiency assessment above. Respondent's computation of the subject undeclared income was arrived at after comparing the total expenses reported in petitioner's

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[146] Exhibit "R-25", BIR Records (Folder 3 of 4), p. 494.

amended audited financial statements and declared in the amended ITR with the total expenses found per audit.[147] The discrepancy, with the declared amount being lesser than the supported expenses, was deemed as undeclared income.

Considering that respondent's foregoing assessment was still based on the presumption that the undeclared expenses constitute undeclared income, which as this Court already ruled to have no legal and factual bases, it necessarily follows the same cannot likewise be considered as sales subject to VAT. Thus, the assessed deficiency VAT based on the deemed undeclared income cannot be sustained.

Disallowed input tax on unsupported purchases

Respondent found that petitioner has unsupported purchases for TY 2012. The corresponding input taxes therefrom in the amount of ₱7,045,577.65. Respondent's computation is shown below:[148]

Purchases per VAT returns filed	₱101,179,854.48
Total per Invoice Summary	42,466,707.40
Unsupported VAT Purchases	₱ 58,713,147.08
Multiply by VAT Rate	12%
Input tax from unsupported purchases	**₱ 7,045,577.65**

Notably, the foregoing computation is adjusted to reflect only the 2nd, 3rd, and 4th quarters of 2012 which are not barred by prescription:

Purchases per VAT returns file	₱101,179,854.48	
Less: Purchases for 1st Quarter[149]	20,069,403.33	₱81,110,451.15
Total per Invoice Summary	₱42,466,707.40	
Less: Total invoices for the 1st Quarter[150]	8,907,569.34	33,559,138.06
Unsupported VAT Purchases for the 2nd, 3rd & 4th quarters		₱ 47,551,313.09
Multiply by VAT Rate		12%
Input tax from unsupported purchases – 2nd to 4th quarters		**₱ 5,706,157.57**

[147] BIR Records (Folder 3 of 4), p. 410.
[148] Exhibit "R-25-A", BIR Records (Folder 3 of 4), p. 491.
[149] BIR Records (Folder 3 of 4), p. 277.
[150] BIR Records (Folder 3 of 4), pp. 432 to 437.

As discussed previously, petitioner was not able to refute respondent's findings by submitting supporting documents and, this fact is bolstered by the ICPA in his report wherein he stated that he was only able to examine supporting documents for petitioner's purchases amounting to ₱1,070,883.18. [151] Thus, he concluded that for TYs 2011 and 2012, "no input tax can be claimed from the purchases supported by supplementary receipts and packing list as these are not valid source of input tax." [152] For such reasons, this item of assessment should be upheld.

Unsupported Certificate of Tax Credit

Respondent's examiner compared the creditable VAT withheld by government agencies from their purchase payments to petitioner per amounts declared in petitioner's VAT returns and BIR Form No. 2306. In doing so, the following discrepancy was found:[153]

Creditable VAT withheld per VAT returns	₱ 511,022.86
Total per BIR No. Form 2306	510,005.08
Unsupported Creditable VAT Withheld	**₱ 1,017.78**

To determine the amount pertaining to the period that is not barred by prescription, the foregoing is adjusted in this wise:

Total Creditable VAT withheld per VAT returns	₱511,022.86	
Less: Creditable VAT withheld for the 1st quarter[154]	176,194.54	₱334,828.32
Total per BIR Form 2306	₱510,005.08	
Less: BIR Form No. 2306 for the 1st quarter[155]	176,194.52	333,810.56
Unsupported Creditable VAT Withheld – 2nd to 4th quarters		**₱ 1,017.76**

Anent the disallowed VAT credits, petitioner alleges in its Legal Petition Notice dated July 10, 2015[156] the following:

> "I believe that there are so many legal remedies to check and verify if the creditable withholding tax truly exists or not. Through access letters, third party contacts/inquiries should be utilized in proving the alleged unsupported creditable withholding taxes. On the other hand, this belief shall not

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151 Exhibit "P-22", Docket – Vol. II, p. 625.
152 Exhibit "P-22", Docket – Vol. II, p. 646.
153 Exhibit "R-25-A", BIR Records (Folder 3 of 4), p. 491.
154 BIR Records (Folder 3 of 4), p. 277.
155 BIR Records (Folder 3 of 4), pp. 400 to 401.
156 Exhibit "P-10-A", Docket – Vol. II, p. 709.

> undermine my right to submit additional certificate of tax credit to support the same."

However, no certificate of tax credit was ever submitted by petitioner. Thus, the disallowance is upheld.

Thus, petitioner is liable for deficiency VAT for TY 2012 in the amount of ₱5,707,175.33, computed as follows:

Unsupported Purchases	₱47,551,313.09
VAT Rate	12%
Disallowed input tax on unsupported purchases	₱ 5,706,157.57
Add: Unsupported Certificate of Tax Credit	1,017.76
Deficiency VAT	**₱ 5,707,175.33**

Petitioner is liable for IAET for TY 2012.

Respondent likewise assessed petitioner of IAET for TY 2012, to wit:[157]

Taxable Income per Audit		₱73,006,749.71
Less: Income Tax paid	₱ 417,926.36	
Amount to be retained (100% Paid-up Capital)	125,000.00	542,926.36
Improperly Accumulated Earnings		₱72,463,823.35
Multiply by IAE Tax Rate		10%
Improperly Accumulated Earnings Tax		₱7,246,382.34
Add: 50% Surcharge	₱3,623,191.17	
20% Interest from 01-25-2013 to 06-22-2015	3,534,624.27	7,157,815.44
Total Deficiency IAET		**₱14,404,197.78**

Again, the Court notes that the foregoing computation starts at the taxable income found by respondent's examiner per audit, and not from petitioner's taxable income for the subject year. However, it is correct that the retained earnings from prior years are not added to the taxable income since they have been added in the IAET computation for TY 2011, pursuant to Section 5 of RR No. 2-2001, which states that "[o]nce the profit has been subjected to IAET, the same shall no

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[157] Exhibit "R-25", BIR Records (Folder 3 of 4), p. 493.

longer be subjected to IAET in later years even if not declared as dividend."

In order not to be subjected to IAET, petitioner should be able to prove that the accumulated earnings are for the reasonable needs of the business. To substantiate its claim, petitioner submitted Board Resolution No. 4 dated February 13, 2014, showing that it reserved the amount of ₱10,400,000.00 for plant expansion.[158] However, as discussed previously, this document alone does not prove that petitioner's earnings were accumulated for the reasonable needs of the business.

Furthermore, per petitioner's comparative financial statements for 2013 and 2012, additions to its *Property, Plant and Equipment* account consist only of ₱500,000.00 for Trucks and Vehicles, and ₱250,000.00 for Office furniture and fixtures.[159] Therefore, the appropriated amount for plant expansion in the previous year was not used for the intended purpose.

Thus, petitioner is liable for IAET in the adjusted amount of ₱315,857.08, as computed below:

Taxable Income per amended ITR[160]		₱4,335,018.00
Less: Income tax paid	₱1,051,447.22	
Amount to be retained (100% Paid-up Capital)	125,000.00	1,176,447.22
Improperly Accumulated Earnings		₱3,158,570.78
Multiply by IAE Tax rate		10%
Improperly Accumulated Earnings Tax		**₱315,857.08**

To recapitulate, petitioner's aggregate deficiency tax liability for TY 2012 amounts to ₱26,697,570.72:

	Tax Deficiency/Liability
Income tax	₱ 20,674,538.31
VAT	5,707,175.33
Improperly Accumulated Earnings Tax	315,857.08
Total	**₱ 26,697,570.72**

[158] Exhibit "P-22", Annex 106.
[159] BIR Records (Folder 2 of 4), p. 82. See also Exhibit "P-22", Annex 127-15.
[160] Exhibit "P-22", Annexes 94-2, 94-3 and 101.

For TY 2013

Petitioner is liable for deficiency income tax for TY 2013.

Respondent's audit reveals the following deficiency income tax from petitioner's unsupported purchases/expenses:[161]

Taxable Income per return		₱5,850,693.00
Add: Unsupported Purchases/Expenses		61,488,201.15
Taxable Income per audit		₱67,338,894.15
Income Tax Due Thereon		₱20,201,668.00
Less: Income Tax Paid per return	₱1,479,596.00	
Income Tax credits per audit	241,146.14	1,720,742.14
Deficiency Income Tax		₱18,480,925.86
Add: 50% Surcharge	₱9,240,462.93	
20% Interest p.a. (04/16/14 to 06/22/15)	4,373,819.12	13,614,282.05
Amount Due/Collectible		**₱32,095,207.91**

It is noted that the amount of petitioner's taxable income for TY 2013 per audited financial statements is ₱5,850,696.89,[162] which is different from the amount used by respondent in the above assessment. As such, the computation of petitioner's deficiency income tax shall be adjusted accordingly.

Unsupported Purchases/Expenses

The breakdown of the unsupported purchases/expenses found by respondent's examiner is as follows:[163]

	Reported per Financial Statements (FS) & VAT Returns	Determined per Audit	Discrepancy
1. Vatable Purchases/Expenses	₱121,022,712.67	₱72,107,223.09	₱48,915,489.58
2. Taxes/Licenses Expense	234,862.08	11,000.00	223,862.08

161 Exhibit "R-16", BIR Records (Folder 2 of 4), p. 599.
162 Exhibit "P-22", Annex 124; BIR Records (Folder 2 of 4), p. 101.
163 Exhibit "R-16-A", BIR Records (Folder 2 of 4), p. 597.

3. Communication/Light/Water	1,020,364.53	23,666.50	996,698.03
4. Fuel/Oil Expense	745,360.83	190,735.22	554,625.61
5. Repairs/Maintenance	445,930.43	285,095.19	160,835.24
6. LTO Registration	69,852.00	9,071.43	60,780.57
7. Supplies Expense	47,855.00	45,561.86	2,293.14
8. Miscellaneous	215,682.02	180,094.66	35,587.36
9. SSS/Pag-ibig/PhilHealth	221,961.40	228,826.44	6,865.04*
10. Insurance Expense	46,335.06	52,916.07	6,581.01*
11. Salaries/Wages Expense	8,542,400.00	50% Disallowed	4,271,200.00
12. Interest Expense	12,281,541.97	50% Disallowed	6,140,770.99
13. Representation	125,225.00	50% Disallowed	62,612.50
14. Donation	100,000.00	50% Disallowed	50,000.00
TOTAL			**₱61,488,201.15**

**Deemed undeclared income.*

First, We discuss petitioner's under declared expenses which are deemed undeclared income by respondent.

From the foregoing table, amounts for SSS/Pag-ibig/PhilHealth and Insurance Expense per audit *exceed* the corresponding amounts reported in petitioner's financial statements for TY 2013 and, thus, deemed as undeclared income:

	Reported per Financial Statements (FS) & VAT Returns	**Determined per Audit**	**Discrepancy**
SSS/Pag-ibig/PhilHealth	₱221,961.40	₱ 228,826.44	₱ 6,865.04
Insurance Expense	46,335.06	52,916.07	6,581.01
TOTAL	**₱268,296.46**	**₱281,742.51**	**₱ 13,446.05**

But as discussed earlier, treating the unaccounted or under-declared expenses as undeclared income results to zero taxable income. Thus, the amount of ₱13,446.05 should be deducted from the total disallowance of ₱61,488,201.15.

Petitioner protested the foregoing disallowances, particularly the computation of the disallowed salaries/wages expense, interest expense, representation, and donation, which were merely multiplied by 50% by respondent:

	Reported per Financial Statements (FS)	Determined per Audit (multiplied by 50%)
Salaries/Wages Expense	₱ 8,542,400.00	₱ 4,271,200.00
Interest Expense	12,281,541.97	6,140,770.99
Representation	125,225.00	62,612.50
Donation	100,000.00	50,000.00
TOTAL	**₱21,049,166.97**	**₱10,524,583.49**

Petitioner alleges in its Legal Petition Notice dated July 10, 2015 for the 2013 assessments the following:[164]

> "**A. Income Tax**
>
> 1. Disallowed Unsupported Expenses (P12,572,711.57)
>
> xxx
>
> b. Further, I believe the application of Best Evidence Obtainable (BEO) Rule which reduces my claimed expenses in half is outrageously misplaced. The rule wherein BEO is based shall be only applied if evidences are not forthcoming and exactitude of expenses cannot be determined. Since there's compliance on my part last July 31, 2014, I believe all evidences are made available for revenue officers' perusal.
>
> xxx"

Unfortunately, petitioner failed to support the foregoing allegations with documentary evidence, as shown in the following findings of the ICPA,[165] to wit:

> "9.7. For the year ended December 31, 2013, as presented under Note 16 of the Notes to Financial Statements, total purchases amounted to ₱128,525,480.25. However, we were only able to examine the following:

	Amount
Purchases with check vouchers and supporting documents	₱ 34,465,507.06
Purchases with no check vouchers but with supporting documents	12,008,133.90
Purchases with check vouchers but no attached supporting documents	1,367,116.00
	₱ 47,840,756.96

> xxx

[164] Exhibit "P-10-B", Docket – Vol. II, p. 715.
[165] Par. 9.7, Exhibit "P-22", Docket – Vol. II, pp. 636 to 638. *am*

9.8. Presented below are the expenses and the amounts with supporting documents:

	Amounts per AFS	Validated with supporting documents	Validated with exceptions	Not Validated
Salaries and other wages	₱ 8,542,400.00	-	-	₱ 8,542,400.00
SSS, Philhealth/ Pag-ibig	221,961.40	-	-	221,961.40
Taxes and licenses	234,862.08	91,250.00	107,155.00	36,457.08
Communication, light and water	1,020,364.53	-	24,737.65	995,626.88
Fuel and oil	745,360.83	-	-	745,360.83
Repairs and maintenance	445,930.43	-	410,165.00	35,765.43
LT[O] registration	69,852.00	60,368.26	-	9,483.74
Insurance expense	46,335.06	-	-	46,335.06
Interest expense	12,281,541.97	-	6,439,226.74	5,842,315.23
Representation expense	125,225.00	-	-	125,225.00
Miscellaneous/other expense	215,682.02	-	-	215,682.02
Donation/contribution	100,000.00	-	100,000.00	-
Supplies Expense	47,855.00	-	-	47,855.00
Depreciation expense	455,643.43	-	-	455,643.43
TOTAL	**₱24,553,013.75**	**₱151,618.26**	**₱7,081,284.39**	**₱17,320,111.10"**

Further, the ICPA concluded that for the TY 2013, the total amount of purchases that had been found to have complied with the requirements of deductibility amounts to ₱10,492,289.91.[166]

From the foregoing, it is clear that petitioner failed to provide supporting documents for all of its declared purchases and expenses to overcome the presumption of correctness of the subject assessment. Thus, the disallowance of unsupported purchases/expenses for TY 2013 is upheld, but in the adjusted amount of ₱61,474,755.10, as computed below:

Total Unsupported Purchases/Expenses per audit	₱ 61,488,201.15
Less: Under declared expenses deemed undeclared income	13,446.05
Adjusted Unsupported Purchases/Expenses	**₱61,474,755.10**

[166] Exhibit "P-22", Docket – Vol. II, p. 645.

Unsupported income tax credits

In the FLD, respondent deducted from the income tax deficiency the amount of ₱241,146.14 as income tax credits per audit.[167] However, petitioner's ITR shows total taxes withheld amounting to ₱275,613.00.[168] Respondent effectively disallowed petitioner's income tax credits for the TY 2013 amounting to ₱34,466.86 for being unsupported:[169]

Per Return	₱275,613.00
Per Withholding Tax Certificates[170]	241,146.14
Unsupported Income Tax Credits	**₱ 34,466.86**

Again, petitioner failed to submit evidence to prove otherwise. Thus, the disallowance is upheld.

In fine, petitioner is liable to deficiency income tax for TY 2013 amounting to ₱18,476,893.46, computed as follows:

Taxable Income as adjusted		₱ 5,850,696.89
Add: Unsupported Purchases/Expenses		61,474,755.10
Taxable Income per audit		₱ 67,325,451.99
Income Tax Due Thereon		₱ 20,197,635.60
Less: Income Tax paid per return	₱1,479,596.00	
Income Tax Credits per audit	241,146.14	1,720,742.14
Deficiency Income Tax		**₱18,476,893.46**

Petitioner is liable for deficiency VAT for TY 2013.

Petitioner was found liable for deficiency VAT for TY 2013 amounting to ₱11,469,857.44, including surcharge and interest:[171]

Vatable Sales per return	₱143,869,595.20	
Add: Undeclared Income	13,446.05	₱143,883,041.25
Output tax thereon		₱ 17,265,964.95

[167] Exhibit "R-16", BIR Records (Folder 2 of 4), p. 599.
[168] BIR Records (Folder 2 of 4), p. 109. [₱132,323.00 + ₱143,290.00]
[169] Exhibit "R-16-A", BIR Records (Folder 2 of 4), p. 597. With ₱1.00 difference per actual ITR.
[170] BIR Records (Folder 2 of 4), pp. 524 to 526.
[171] Exhibit "R-16", BIR Records (Folder 2 of 4), p. 599.

Less: Input Tax (IT) per audit		
Amount per return	₱ 15,679,432.33	
Less: Unsupported IT on discrepancy on claimed vatable purchases/expenses (P48,915,489.58 x 12%)	5,869,858.75	9,809,573.58
VAT Due Thereon		₱ 7,456,391.37
Less: VAT paid/return	₱ 309,148.22	
VAT credits per audit	707,522.82	1,016,671.04
Deficiency VAT		₱ 6,439,720.33
Add: 50% Surcharge	₱ 3,219,860.17	
20% Interest p.a. (01/26/14 to 06/22/15)	1,810,276.94	5,030,137.11
Amount Due/Collectible		**₱11,469,857.44**

From the foregoing, the items of assessment are undeclared income, disallowed input taxes, and disallowed VAT credits, which will be discussed in detail hereafter.

Output tax from undeclared income

This amount comes from the under declared expense deemed undeclared income in the income tax assessment.[172] Considering that the Court has already cancelled this item from the income tax assessment, the same cannot be a valid ground for VAT assessment. An expense cannot give rise to output tax, hence, this item of assessment should be cancelled.

Disallowed input taxes

Likewise, this item of assessment comes from the unsupported purchases found per audit:[173]

Reported per Financial Statements (FS) & VAT Returns	₱121,022,712.67
Determined per audit	72,107,223.09
Unsupported VATable Purchases	₱48,915,489.58
Multiply by VAT rate	12%
Disallowed input taxes on unsupported purchases	**₱5,869,858.75**

The ICPA reported:[174]

[172] Exhibit "R-16-A", BIR Records (Folder 2 of 4), p. 597.
[173] Exhibit "R-16-A", BIR Records (Folder 2 of 4), p. 597.
[174] Exhibit "P-22", Docket – Vol. II, p. 646.

"As of December 31, 2013, the amount of input tax that can be claimed amounts to ₱1,195,022.19."

Since petitioner failed to submit evidence to fully substantiate its purchases for TY 2013, this disallowance is upheld.

Disallowed VAT credits

Petitioner declared creditable VAT withheld per VAT returns in the amount of ₱1,226,148.89.[175] However, respondent's audit showed VAT credits supported by certificates of VAT withheld in the amount of ₱707,522.82.[176] Effectively, respondent disallowed ₱518,626.07 of unsupported VAT credits. This is unrefuted by petitioner. Thus, the Court should not disturb the same.

Respondent also deducted from the deficiency VAT the payments already made by petitioner amounting to ₱309,148.22. On the other hand, scrutiny of the BIR Records reveals that per Taxpayer Ledger Inquiry for VAT for the year 2013 in respondent's accounting system, petitioner made payments in the total amount of ₱548,196.43, broken down as follows:[177]

Transaction Date	Transaction Type	Amount
February 20, 2013	PYT	₱ 17,310.04
March 20, 2013	PYT	18,175.55
April 25, 2013	PYT	19,845.64
May 20, 2023	PYT	20,837.93
June 20, 2023	PYT	25,005.52
August 20, 2013	PYT	27,143.15
September 20, 2013	PYT	25,718.43
October 25, 2013	PYT	28,295.74
November 20, 2013	PYT	31,125.33
December 20, 2013	PYT	68,435.15
January 27, 2014	PYT	266,303.95
	TOTAL	**₱548,196.43**

175 BIR Records (Folder 2 of 4), p. 97.
176 BIR Records (Folder 2 of 4), pp. 524 to 526.
177 BIR Records (Folder 2 of 4), p. 64.

Hence, petitioner's deficiency VAT liability for the TY 2013 amounts to ₱6,199,058.59, computed as follows:

VATable Sales per return		₱143,869,595.20
Output tax thereon		₱ 17,264,351.42
Less: Input tax per audit		
Amount per return	₱ 15,679,432.33	
Less: Unsupported IT on discrepancy	5,869,858.75	9,809,573.58
VAT Due		₱ 7,454,777.84
Less: VAT Paid/return	₱ 548,196.43	
VAT Credits per audit	707,522.82	1,255,719.25
Deficiency VAT		**₱ 6,199,058.59**

In fine, petitioner's total deficiency tax liability for TY 2013 is in the aggregate amount of ₱24,675,952.05:

	Tax Deficiency/Liability
Income tax	₱ 18,476,893.46
VAT	6,199,058.59
Total	**₱ 24,675,952.05**

WHEREFORE, in light of the foregoing considerations, the present *Petition for Review* is **PARTIALLY GRANTED**.

Accordingly, **for TY 2011**, the assessment issued by respondent against petitioner covering the deficiency VAT is **CANCELLED**, while the deficiency income tax, IAET and the annual registration fee is **PARTIALLY UPHELD**.

For TY 2012, the assessment issued by respondent against petitioner covering the deficiency income tax, VAT and IAET is **PARTIALLY UPHELD**.

For TY 2013, the assessment issued by respondent against petitioner covering the deficiency income tax and VAT is **PARTIALLY UPHELD**.

Petitioner is thus **ORDERED TO PAY** respondent the aggregate amount of **₱165,427,503.60**, representing deficiency taxes for TYs 2011 to 2013, inclusive of twenty-five percent (25%) surcharge imposed under Section 248(A)(3) of the 1997 NIRC, as amended, and deficiency interest imposed under

Section 249(B) of the same Code, respectively, computed until January 22, 2019,[178] computed as follows:

Taxable Year 2011	**Income tax**		**IAET**	**TOTAL**
Basic deficiency tax	₱19,418,171.92		₱738,765.44	₱20,156,937.36
Add: 25% Surcharge	4,854,542.98		184,691.36	5,039,234.34
Add: Deficiency Interest				
Income Tax:				
20% Deficiency Interest from April 16, 2012 to December 31, 2017 (₱19,418,171.92 x 20% x 2086/365 days)	22,195,236.51			22,195,236.51
12% Deficiency Interest from January 1, 2018 to January 22, 2019 (₱19,418,171.92 x 12% x 387/365 days)	2,470,629.87			2,470,629.87
IAET:				
20% Deficiency Interest from January 16, 2013 to December 31, 2017 (₱738,765.44 x 20% x 1811/365 days)			733,098.20	733,098.20
12% Deficiency Interest from January 1, 2018 to January 22, 2019 (₱738,765.44 x 12% x 387/365 days)			93,995.25	93,995.25
Total amount due, Jan. 22, 2019	**₱48,938,581.28**		**₱1,750,550.25**	**₱50,689,131.53**
Taxable Year 2012	**Income tax**	**VAT**	**IAET**	**TOTAL**
Basic deficiency tax	₱20,674,538.31	₱5,707,175.33	₱315,857.08	₱26,697,570.72
Add: 25% Surcharge	5,168,634.58	1,426,793.83	78,964.27	6,674,392.68
Add: Deficiency Interest				
Income Tax:				
20% Deficiency Interest from April 16, 2013 to December 31, 2017 (₱20,674,538.31 x 20% x 1721/365 days)	19,496,372.84			19,496,372.84
12% Deficiency Interest from January 1, 2018 to January 22, 2019 (₱20,674,538.31 x 12% x 387/365 days)	2,630,480.98			2,630,480.98
VAT:				
20% Deficiency Interest from January 26, 2013 to December 31, 2017 (₱5,707,175.33 x 20% x 1801/365 days)		5,632,122.07		5,632,122.07
12% Deficiency Interest from January 1, 2018 to January 22, 2019 (₱5,707,175.33 x 12% x 387/365 days)		726,140.34		726,140.34
IAET:				

[178] Exhibit "R-30", BIR Records (Folder 4 of 4), p. 33. The *Final Notice Before Seizure* dated January 15, 2019, which was received by petitioner on January 17, 2019, states: "You are again advised to settle your tax liability within 5 days from receipt of this letter to avoid accumulation of delinquency interest." Thus, petitioner's tax liabilities became due on January 22, 2019.

20% Deficiency Interest from January 16, 2014 to December 31, 2017 (₱315,857.08 x 20% x 1446/365 days)			250,262.65	250,262.65
12% Deficiency Interest from January 1, 2018 to January 22, 2019 (₱315,857.08 x 12% x 387/365 days)			40,187.40	40,187.40
Total amount due, Jan. 22, 2019	**₱47,970,026.71**	**₱13,492,231.57**	**₱685,271.40**	**₱62,147,529.68**
Taxable Year 2013	**Income tax**	**VAT**		**TOTAL**
Basic deficiency tax	₱18,476,893.46	₱6,199,058.59		₱24,675,952.05
Add: 25% Surcharge	4,619,223.36	1,549,764.65		6,168,988.01
Add: Deficiency Interest				
Income Tax:				
20% Deficiency Interest from April 16, 2014 to December 31, 2017 (₱18,476,893.46 x 20% x 1356/365 days)	13,728,584.95			13,728,584.95
12% Deficiency Interest from January 1, 2018 to January 22, 2019 (₱18,476,893.46 x 12% x 387/365 days)	2,350,868.31			2,350,868.31
VAT:				
20% Deficiency Interest from January 26, 2014 to December 31, 2017 (₱6,199,058.59 x 20% x 1436/365 days)		4,877,725.01		4,877,725.01
12% Deficiency Interest from January 1, 2018 to January 22, 2019 (₱6,199,058.59 x 12% x 387/365 days)		788,724.06		788,724.06
Total amount due, January 22, 2019	**₱39,175,570.08**	**₱13,415,272.31**		**₱52,590,842.39**
TOTAL-Taxable years 2011 to 2013	**₱136,084,178.07**	**₱26,907,503.88**	**₱2,435,821.65**	**₱165,427,503.60**

In addition, petitioner is also **ORDERED TO PAY** the annual registration fees for TY 2011 for all of its four (4) branches in the amount of **₱2,000.00** plus the applicable surcharge and interests.

Finally, petitioner is **ORDERED TO PAY** respondent delinquency interest at the rate of twelve percent (12%) on the total unpaid deficiency taxes of **₱165,427,503.60** as of January 22, 2019 for TYs 2011 to 2013, as determined above, or equivalent to the amount of **₱54,387.12**[179] per day, computed from January 23, 2019 until full payment thereof, pursuant to Section 249(C) of the 1997 NIRC, as amended by

[179] ₱165,427,503.60 times 12% divided by 365 days.

RA No. 10963 or the Tax Reform for Acceleration and Inclusion Law and implemented by RR No. 21-2018.

SO ORDERED.

Catherine T. Manahan
CATHERINE T. MANAHAN
Associate Justice

WE CONCUR:

ROMAN G. DEL ROSARIO
Presiding Justice

Marian Ivy F. Reyes-Fajardo
MARIAN IVY F. REYES-FAJARDO
Associate Justice

CERTIFICATION

Pursuant to Article VIII, Section 13 of the Constitution, 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