REPUBLIC OF THE PHILIPPINES
Court of Tax Appeals
QUEZON CITY

Third Division

WILLIAM R. VILLARICA, *Petitioner,*	**CTA CASE NO. 9343**
	Members:
-versus-	**UY,** *Chairperson,* **RINGPIS-LIBAN,** *and* **MODESTO-SAN PEDRO,** *JJ.*
COMMISSIONER OF INTERNAL REVENUE,	Promulgated:
Respondent.	OCT 2 1 2021 2:12 p.m.

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DECISION

MODESTO-SAN PEDRO, J.:

The Case

This is a Petition for Review,[1] filed by petitioner William R. Villarica on 5 May 2016 pursuant to ***Section 3(a)(1), Rule 4 of the Revised Rules of the Court of Tax Appeals ("RRCTA")***.[2] He prays for the Court to cancel and set aside the Final Decision on Disputed Assessment ("FDDA"), dated 4 April 2016, issued against him by respondent Commissioner of Internal Revenue ("CIR").

In the FDDA, respondent found petitioner liable for deficiency income tax and value-added tax ("VAT"), inclusive of interest and surcharge, for taxable years 1998, 2000, 2001, 2006, 2007, 2008, and 2009, in the aggregate amount of ₱112,105,286.68.

The Parties

Petitioner William R. Villarica is a Filipino of legal age. He may be served with summons and other court processes through his counsel with office address at the 8th Floor, One Corporate Plaza, 845 Arnaiz Avenue, Makati City, Metro Manila.

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1 Petition for Review, Division Records Vol. 1, pp. 10-150 with annexes.
2 A.M. No. 05-11-07-CTA, 22 November 2005.

Respondent Commissioner of Internal Revenue is the duly appointed Commissioner of the Bureau of Internal Revenue ("BIR") who has the power to decide on disputed assessments, fees or other charges and penalties imposed in relation thereto, or other matters arising under the ***National Internal Revenue Code of 1997, as amended (hereinafter referred to as the "Tax Code")***, or other laws or portions thereof administered by the BIR. He holds office at the BIR National Office Building, Agham Road, Diliman, Quezon City.

The Facts

On 8 May 2007, the BIR received an anonymous letter from a concerned citizen, dated 4 May 2007. In the said letter, the concerned citizen narrated that petitioner owns W. Villarica Pawnshops where he/she was previously employed. He/she also alleged that petitioner owns several luxury vehicles. Notwithstanding his business and assets, he/she claimed that petitioner has not been paying taxes.[3]

On account of the said letter, the BIR National Investigation Division ("NID") conducted a preliminary investigation against petitioner. The NID was able to obtain the following information:

a. Petitioner was registered in Revenue District Office ("RDO") No. 52 as a Single Proprietor-Pawnshop Operator from 26 September 1991 until 2008;[4]

b. Petitioner's Annual Income Tax Returns ("ITR") for taxable years 1999, 2000, 2001, and 2007 were not among those received and encoded by the Document Processing Section of RDO No. 52;[5]

c. As per the computer records of RDO No. 52, petitioner has not filed any ITR since taxable year 1999;[6]

d. Petitioner filed his ITR for taxable years 1999 to 2001 in RDO No. 25;[7]

e. RDO 25B has no records of petitioner's ITR for taxable years 2002 to 2006, 2008, and 2009;[8]

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[3] Exhibit "R-1" to "R-1-A", BIR Records Folder 3, p. 315.
[4] Exhibit "R-2", Division Records Vol. 5, p. 2185.
[5] *Ibid.*
[6] *Ibid.*
[7] *Ibid.*
[8] Exhibit "R-3" and "R-5, *id.*, pp. 2186-2187.

f. Petitioner filed his ITR for taxable year 2007 in RDO No. 25. In the said ITR, the words "NO OPERATION" and "NIL" were typewritten on spaces nos. 26A- the Gross Taxable Compensation Income and 43C-Aggregate Amount Payable/(Overpayment), respectively;[9]

g. Certain vehicles are registered under petitioner's name, specifically, a Volkswagen Beetle amounting to ₱1,500,000.00,[10] a Toyota MR2 Spyder amounting to ₱2,350,000.00,[11] a Toyota Super Grandia amounting to ₱1,180,000.00,[12] a Ferrari Coupe amounting to ₱40,000,000.00,[13] and a Lamborghini Gallardo amounting to ₱26,000,000.00;[14]

Taking cue from the foregoing, the BIR issued Letter of Authority No. LOA200900044653 ("LOA") on 14 July 2010. The LOA authorized Revenue Officers ("RO") A.M. Simpit, L. Sante, G. Saga, G. Eito, and Group Supervisor ("GS") Aurora V. Flor, all from the NID, to examine the books of accounts and other accounting records of petitioner. The LOA covered all types of internal revenue taxes for "Calendar Year 2009 and unverified prior years".[15]

The next day, the BIR filed a Joint Complaint-Affidavit with the Department of Justice ("DOJ") charging petitioner for violation of ***Sections 254 and 255 of the Tax Code.***[16] The case was docketed as XVI-INV-10G-00225 entitled BIR v. Villarica.

Thereafter, the BIR sent the following Notices requesting petitioner to present his books of accounts and other accounting records in relation to the LOA, to wit:

Notice	Date of Notice	Date Received by Petitioner
Second Notice[17]	12 August 2010	20 August 2010
Final Notice[18]	28 September 2010	4 October 2010

9 Exhibit "R-4", BIR Records Folder 5, pp. 603-604.
10 Exhibit "R-6" to "R-9", Division Records Vol. 5, pp. 2188-2191.
11 Exhibit "R-10" and "R-12", *id.*, pp. 2192-2193.
12 Exhibit "R-13" to "R-14", *id.*, pp. 2194-2195.
13 Exhibit "R-15", *id.*, p. 2196; Exhibit "R-16" to "R-19", BIR Records Folder 5, pp. 565, 597-598.
14 Exhibit "R-21" to "R-23", BIR Records Folder 1, pp. 68, 70-71.
15 Exhibit "R-24", Division Records Vol. 5, p. 2197; Exhibit "P-15", Division Records Vol. 3, p. 1396.
16 Exhibit "P-12", Division Records Vol. 3, pp. 1367-1395; CIR Letter to DOJ, BIR Records Folder 5, pp. 748-749.
17 Exhibit "R-29", *id.*, pp. 734-736.
18 Exhibit "R-30", *id.*, p. 740.

On 22 February 2011, the BIR issued a Notice of Informal Conference inviting petitioner to discuss the ongoing audit investigation against him on 28 February 2011.[19]

On 15 March 2011, the BIR issued a Second Notice of Informal Conference reiterating its invitation to petitioner scheduled on 16 March 2011.[20] The Second Notice of Informal Conference was received by him on 16 March 2011.[21]

Continuing its investigation, the BIR secured additional documents from the Securities and Exchange Commission and the Local Government of Marilao, Bulacan, which include:

a. Certificate of Incorporation and Articles of Incorporation of Villarica Country Homes, Inc. to which petitioner is an incorporator;[22]

b. General Information Sheet of Villarica Country Homes, Inc for 2009 where it is indicated that petitioner is the President of the said company and owns ₱100,000.00 out of the company's total ₱2,200,500.00 paid-up capital;[23]

c. Business Permit of Villarica Country Homes in the Municipality of Marilao, Bulacan for year 2008 showing the company's declared capital investment of ₱1,000,000.00;[24]

d. Business Permit of the Marilao Coliseum/Villarica Willam in the Municipality of Marilao, Bulacan for year 2010 showing the business' capital investment of ₱500,000.00;[25]

e. Deed of Sale of a Ferrari, dated 15 May 2013, in the amount of ₱15,000,000.00 sold by William R. Villarica to Lilibeth B. Respensor; and[26]

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19 Exhibit "R-31", Division Records Vol. 5, p. 2198.
20 Exhibit "R-32", BIR Records Folder 3, pp. 279-280.
21 *Ibid.*
22 Exhibit "R-25", BIR Records Folder 3, pp. 321-327.
23 Exhibit "R-26", *id.*, pp. 355-363.
24 Exhibit "R-27", BIR Records Folder 1, p. 36.
25 Exhibit "R-28", BIR Records Folder 5, p. 587.
26 Exhibit "R-37", *id.*, p. 577.

f. Deed of Sale of a Lamborghini, dated 22 August 2007, in the amount of ₱20,000,000.00 sold by William R. Villarica to Ryan Jeffrey S. Son.[27]

Based on the foregoing findings, the BIR issued an undated Preliminary Assessment Notice ("PAN") which was received by petitioner on 1 June 2011.[28] In the PAN, he was assessed for deficiency income tax and VAT for taxable years 1998, 2000, 2001, 2006-2009 in the aggregate amount (including interests and surcharge) of ₱79,280,794.55.[29] The assessments arose from petitioner's alleged unaccounted source of cash broken down, as follows:

INCOME TAX			
Taxable Year	**Basis of Assessment**	**Tax Base**	**Total Tax Due (incl. of interest, penalty and surcharge)**
1998	Purchase of Volkswagen	₱ 1,500,000.00	₱ 1,823,396.09
2000	Purchase of Toyota MR2 Spyder	2,350,000.00	2,458,111.03
2001	Purchase of Toyota Grandia	1,180,000.00	1,144,815.89
2006	Purchase of Ferrari Coupe	40,000,000.00	29,889,917.81
2007	Purchase of Lamborghini	26,000,000.00	17,742,762.56
2008	Cap. Invest. in Villarica Country Homes	1,000,000.00	553,342.47
2009	Cockpit Arena Improvements	7,006,628.00	3,843,817.05
TOTAL		**₱ 79,036,628.00**	**₱ 57,456,162.90**
VALUE-ADDED TAX			
Taxable Year	**Basis of Assessment**	**Tax Base**	**Total Tax Due (incl. of interest, penalty and surcharge)**
1998	Purchase of Volkswagen	₱ 1,500,000.00	₱ 600,000.00
2000	Purchase of Toyota MR2 Spyder	2,350,000.00	846,000.00
2001	Purchase of Toyota Grandia	1,180,000.00	401,200.00
2006	Purchase of Ferrari Coupe	40,000,000.00	11,360,000.00
2007	Purchase of Lamborghini	26,000,000.00	6,864,000.00
2008	Cap. Invest. in Villarica Country Homes	1,000,000.00	240,000.00
2009	Cockpit Arena Improvements	7,006,628.00	1,513,431.65
TOTAL		**₱ 79,036,628.00**	**₱ 21,824,631.65**
TOTAL AMOUNT DUE			**₱ 79,280,794.55**

[27] Exhibit "R-38", Division Records Vol. 5, p. 2199.
[28] Exhibit "P-3", Division Records Vol. 3, pp. 1274-1276.
[29] Exhibit "R-33", BIR Records Folder 3, pp. 271-276; Exhibit "P-2", Division Records Vol. 3, pp. 1271-1273.

Petitioner sent a Reply to the Preliminary Assessment Notice to the BIR, dated 15 June 2011, disputing the PAN.[30] The letter was sent via registered mail on 16 June 2011 and was received by the BIR on 5 July 2011.[31]

On 16 June 2011, the BIR issued the Formal Letter of Demand ("FLD") with Assessment Notices, where it reiterated and demanded the payment of the assessed deficiency income tax and VAT. The FLD was received by petitioner on 29 June 2011.[32]

Petitioner filed his Protest to the FLD by way of Request for Reconsideration on 29 July 2011.[33] The same was received by the BIR on 16 August 2011.[34]

On 4 April 2016, respondent issued the FDDA which was received by petitioner on 5 April 2016.[35] In the said issuance, he denied petitioner's Protest to the FLD and demanded the payment of the deficiency taxes plus interests and surcharge which, at this time, totaled to ₱112,105,286.68.[36]

Undeterred, petitioner filed his Petition for Review with Motion/Application for Suspension of Tax Collection with this Court on 5 May 2016.[37]

Respondent filed his Answer[38] on 15 August 2016.[39]

In response, petitioner filed a Reply on 30 August 2016,[40] which was admitted by the Court on 6 September 2016.[41]

Thereafter, respondent elevated the BIR Records on 14 October 2016.[42]

Subsequently, petitioner and respondent filed their respective Pre-Trial Briefs on 10 November 2016[43] and 15 November 2016.[44]

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30 Exhibit "P-3", Division Records Vol. 3, pp. 1274-1276.
31 Exhibit "R-39-F", BIR Records Folder 7, pp. 969-973.
32 Exhibits "R-34" to "R-35-M", BIR Records Folder 3, pp. 251-270; Exhibit "P-5" to "P-6", Division Records Vol. 3, pp. 1298-1325.
33 Exhibit "P-6", *id.*, pp. 1318-1325.
34 Exhibit "R-39-F"; BIR Records Folder 7, pp. 953-960.
35 Exhibit "R-36"; *id.*, pp. 1068-1073; Exhibit "P-7", Division Records Vol. 3, pp. 1338-1343.
36 *Ibid.*
37 Petition for Review, Division Records Vol. 1, pp. 10-150 with annexes.
38 Answer, *id.*, pp. 172-183.
39 Resolution dated 22 July 2016, *id.*, p. 171.
40 Reply, *id.*, pp. 190-199.
41 Resolution dated 6 September 2016, *id.*, p. 201.
42 Manifestation, *id.*, pp. 206-208.
43 Petitioner's Pre-Trial Brief, *id.*, pp. 210-219.
44 Respondent's Pre-Trial Brief, Division Records Vol. 2, pp. 594-598.

The Pre-Trial Conference ensued on 15 November 2016.[45] Afterwards, the parties submitted their Joint Stipulation of Facts and Issues on 2 February 2017.[46] This prompted the issuance of the Pre-Trial Order on 22 February 2017.[47]

Meanwhile, the hearing on petitioner's Motion/Application for Suspension of Tax Collection took place on 7 February 2017,[48] 6 March 2017,[49] and 27 June 2017.[50]

During the said hearing, petitioner testified[51] on the following points:

a. He confirmed that he was the owner of several pawnshop branches under the name and style "W. Villarica Pawnshop".

b. He alleged that the same has ceased business operations since 2001 due to the property relations dispute against his former wife.

c. He explained that he had no realized income during the years 2001 to 2009 and was living off his savings.

d. He denied purchasing and owning a Ferrari Coupe and a Lamborgini.

e. He denied signing any Deed of Sale pertaining to the purchase or sale of a Lamborgini.

f. He insisted that the basis of the BIR's assessments which is his supposed "unaccounted source of cash" is incorrect;

g. He asserted that the assessments issued against him are without factual and legal basis; and

h. He testified on the administrative and judicial actions he undertook in contesting the assessments issued against him.

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45 Minutes of the Hearing, *id.*, p. 599; Order, *id.*, pp. 604-604-a.
46 Joint Stipulation of Facts and Issues, *id.*, pp. 624-630.
47 Pre-Trial Order, *id.*, pp. 687-692.
48 Minutes of the Hearing, *id.*, p. 652; Order, *id.*, pp. 653-654.
49 *Id.*, p. 693-695.
50 *Id.*, p. 803-805.
51 Exhibit "P-22", *id.*, pp. 631-651.

Thereafter, petitioner posted his Formal Offer of Documentary Evidence (Re: Motion to Suspend Collection of Taxes) on 22 August 2017.[52] Respondent filed his Comment (on Petitioner's Formal Offer of Evidence dated August 22, 2017) on 29 August 2017.[53]

The trial for the main case proceeded on 4 September 2017.[54]

Petitioner was recalled as witness, and he identified additional documents for the purpose of proving that his signature in the Deeds of Sale in relation to the purchase and sale of the Lamborgini were forgeries.[55] He also manifested that he was adopting his testimony during the Motion/Application for Suspension of Tax Collection in the main case.[56]

He then filed his Formal Offer of Evidence on 19 September 2017.[57] Respondent filed his Comment (on Petitioner's Formal Offer of Evidence dated September 19, 2017) on 25 September 2017.[58] Petitioner filed a Reply on 9 October 2017.[59]

On 26 January 2018, the Court issued a Resolution[60] on petitioner's Formal Offer of Documentary Evidence (Re: Motion to Suspend Collection of Taxes) admitting all pieces of evidence offered except for the following:

Exhibit	Description	Reason for Denial
"P-27"	Annual ITR of petitioner for 2014	For failure to submit duly marked exhibit
"P-28"	Annual ITR of petitioner for 2015	

Meanwhile, the Court deferred the resolution of the Formal Offer of Evidence pertinent to the main case.[61]

On 31 January 2018, respondent filed his Motion to Withdraw BIR Records.[62] Respondent asked the Court to allow him to pull out the BIR records in preparation for his initial presentation of evidence and pre-marking of exhibits.

52 Formal Offer of Documentary Evidence, Division Records Vol. 3, pp. 1043-1241.
53 Comment (on Petitioner's Formal Offer of Evidence dated 22 August 2017), *id.*, 1243-1246.
54 Minutes of the Hearing, *id.*, p. 1247; Order, *id.*, p. 1248.
55 Exhibit "P-32", Division Records Vol. 2, pp. 814-825
56 TSN dated 10 July 2017, p. 4; Minutes of the Hearing, *id.*, p. 826.
57 Formal Offer of Evidence, Division Records Vol. 3, pp. 1263-1416.
58 Comment (on Petitioner's Formal Offer of Evidence dated September 19, 2017), *id.*, pp. 1417-1419.
59 Reply, *id.*, pp. 1425-1441.
60 Resolution dated 26 January 2018, *id.*, pp. 1443-1445.
61 *Ibid.*
62 Motion to Withdraw BIR Records, *id.*, pp. 1446-1449.

On 13 February 2018, petitioner filed a Motion for Partial Reconsideration on the Court's Resolution dated 26 January 2018. He prayed for the Court to allow the admission of "P-27" and "P-28" into evidence.[63]

On 21 February 2018, the Court issued a Resolution denying petitioner's Motion for Suspension of Tax Collection. The Court found that petitioner failed to prove that the collection of the disputed tax assessments will jeopardize his and/or the government's interest since he was not able to prove that the collection of the tax will leave him with no means of income and livelihood.[64]

In the same Resolution, the Court granted respondent's Motion to Withdraw BIR Records.[65]

Aggrieved, petitioner filed his Motion for Reconsideration on the Court's denial of the Motion/Application for Suspension of Tax Collection on 13 March 2018.[66] Respondent filed his Comment/Opposition (to Petitioner's Motion for Reconsideration) on 6 April 2018.[67] The said Motion was denied by this Court on 18 April 2018.[68] This prompted petitioner to file a Petition for *Certiorari* with the Supreme Court, docketed as G.R. No. 240136.[69]

Respondent returned the BIR Records to the Court on 6 April 2018.[70]

On 30 July 2018, the Court issued a Resolution granting (a) petitioner's Formal Offer of Evidence in connection to the main case; and (b) Motion for Partial Reconsideration pertinent to the Formal Offer of Evidence in relation to petitioner's Motion for Suspension of Tax Collection filed on 13 February 2018.[71]

On 5 March 2019, petitioner manifested that he was acquitted in ***CTA Criminal Case No. O-212*** entitled ***People v. Villarica*** **(hereinafter referred to as "CTA Criminal Case")** after the Court of Tax Appeals declared the assessments (which are the same contended assessments in this case) issued against him void. The said criminal case emanated from the aforementioned Joint Complaint filed by respondent with the DOJ.[72]

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63 Motion for Reconsideration, *id.*, pp. 1450-1479.
64 Resolution dated 21 February 2018, *id.*, pp. 1481-1493.
65 *Ibid.*
66 Motion for Reconsideration, *id.*, pp. 1496-1500.
67 Comment/Opposition (to Petitioner's Motion for Reconsideration), Division Records Vol. 4, pp.1508-1512.
68 Resolution dated 18 April 2018, *id.*, pp. 1521-1523.
69 Notice, Division Records Vol. 5, p. 2200.
70 Compliance, Division Records Vol. 4, pp. 1504-1507.
71 Resolution dated 30 July 2018, *id.*, pp. 1891-1893.
72 Manifestation, *id.*, pp. 1918-1920.

On this ground, respondent filed a Motion to Inhibit and Re-Raffle on 15 March 2019.[73] Petitioner filed his Comment/Opposition thereto on 1 April 2019.[74] The Court denied the Motion on 20 May 2019.[75]

On 4 June 2019, respondent filed a Motion for Reconsideration [re: Resolution dated 20 May 2019].[76] Thereafter, petitioner filed his Comment/Opposition [Re: Motion for Reconsideration dated 3 June 2019] on 3 July 2019.[77] On 13 September 2019, the Court denied respondent's Motion.[78] This prompted respondent to file a Petition for *Certiorari* with the Supreme Court, docketed as G.R. No. 250514. The High Court denied the said Petition for lack of merit.[79]

Subsequently, respondent presented his witness, RO Angela Marie S. De Leon on 5 December 2019[80] and 16 January 2020.[81] She testified on the events that transpired during the audit investigation of petitioner as well as the procedures performed by the NID in coming up with the assessments.[82]

Thereafter, respondent filed his Formal Offer of Evidence on 10 February 2020.[83] Petitioner posted his Comment/Objection [Re: Formal Offer of Evidence dated 10 February 2020] on 17 February 2020.[84]

On 24 July 2020, the Court admitted respondent's pieces of evidence except for "R-14", which pertains to an invoice of a Toyota Super Grandia, for being a mere photocopy. In the same Resolution, the Court granted the parties 30 days to file their respective Memoranda.[85]

Petitioner and Respondent posted their respective Memoranda on 8 October 2020[86] and 21 September 2020.[87]

Thereafter, the case was submitted for decision on 22 October 2020.[88] Hence, this Decision.

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73 Motion to Inhibit and Re-Raffle, *id.*, pp. 1930-1935.
74 Comment/Opposition, *id.*, pp. 1941-1944.
75 Resolution dated 20 May 2019, *id.*, pp. 1954-1959.
76 Motion for Reconsideration [re: Resolution dated 20 May 2019], *id.*, pp. 1966-1971.
77 Comment/Opposition [Re: Motion for Reconsideration dated 3 June 2019], *id.*, pp. 1993-1998.
78 Resolution dated 13 September 2019, *id.*, pp. 2001-2004.
79 Notice, Division Records Vol. 5, pp. 2219a-2219d.
80 Minutes of the Hearing, *id.*, p. 2005; Order, *id.*, p. 2006.
81 *Id.*, p. 2095-2097.
82 Exhibit "R-40", Division Records Vol. 4, pp. 1532-1547.
83 Formal Offer of Evidence, Division Records Vol. 5, pp. 2175-2199.
84 Comment/Objection [Re: Formal Offer of Evidence dated 10 February 2020], *id.*, pp. 2201-2214.
85 Resolution dated 24 July 2020, *id.*, pp. 2218-2219.
86 Petitioner's Memorandum, *id.*, pp. 2234-2260.
87 Respondent's Memorandum, *id.*, pp. 2217-2233.
88 Resolution dated 22 October 2020, *id.*, p. 2262.

<u>The Issues</u>[89]

WHETHER RESPONDENT IS AUTHORIZED TO CONDUCT THE INTERNAL REVENUE INVESTIGATION AND EXAMINATION AGAINST PETITIONER WHEN HE ACTED IN VIOLATION OF SECTION 6 OF THE TAX CODE, AS AMENDED, AND REVENUE MEMORANDUM ORDER ("RMO") NO. 43-90 BY ISSUING AND ACTING UNDER AN LOA COVERING "CALENDAR YEAR 2009 AND UNVERIFIED PRIOR YEARS";

WHETHER THE ASSESSMENTS AND THE CORRESPONDING FDDA ARE VOID AND WITHOUT EFFECT FOR BEING IN VIOLATION OF THE TAX CODE, AND THE BIR RULES AND REGULATIONS;

WHETHER RESPONDENT FAILED TO STATE THE LEGAL AND FACTUAL BASES OF THE ASSESSMENTS;

WHETHER PETITIONER IS LIABLE FOR THE ASSESSED DEFICIENCY TAXES; AND

WHETHER THE TAX ASSESSMENTS AGAINST PETITIONER HAVE ALREADY PRESCRIBED UNDER THE LAW.

<u>Arguments of the Parties</u>

<u>Petitioner's Arguments</u>[90]

Petitioner contends that the BIR has no authority to investigate him alleging that the LOA herein is invalid. He explains that the coverage of the said instrument, specifically, "Calendar Year 2009 and unverified prior years" runs contrary to the mandate of ***RMO No. 43-90***,[91] as interpreted in ***CIR v. Sony Philippines, Inc. (hereinafter referred to as the "Sony Case")***,[92] which prohibits the issuance of LOAs covering more than one taxable period. Consequently, he insists that the resulting assessments issued against him are void. h

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[89] *See* Issues in Pre-Trial Order, pp. 2-3, Division Records Vol. 2, pp. 688-689.
[90] Petitioner's Memorandum, Division Records Vol. 5, pp. 2234-2260.
[91] Amendment of Revenue Memorandum Order No. 37-90 Prescribing Revised Policy Guidelines for Examination of Returns and Issuance of Letters of Authority to Audit, 20 September 1990.
[92] G.R. No. 178697, 17 November 2010.

He belies respondent's argument that the ***Sony Case*** does not apply in this case on account of the BIR's findings of fraud against petitioner. He explains that he was able to adduce sufficient evidence disproving respondent's findings which coincides with the ruling in the ***CTA Criminal Case***.

Petitioner stresses that the assessments are bereft of any basis. He contends that the said issuances only contain baseless and general assertions without citing any specific provision of law that he supposedly violated, which is contrary to the requirements under ***Revenue Regulation ("RR") No. 12-99***.[93]

He states that nothing on record shows any factual basis that would establish the existence of his alleged unaccounted source of cash. More so, he insists that respondent failed to show proof that the said unaccounted source of cash amounted to undeclared income. He opines that the presumption of correctness of the assessment does not hold water. He explains that the assessments issued against him are not based on evidence but only on unverified third-party information.

He reiterates that he had no taxable income during the contested periods, considering the closure of his pawnshop business in 2001. He opines that he was merely living off of his savings. He denies having owned a Ferrari Coupe and Lamborghini. He points out that he was able to present sufficient evidence to prove that the signature in the Deeds of Sale pertinent to the Lamborghini are forgeries. He posits that this fact was never countered by respondent. As for the other vehicles registered under his name, petitioner explains that the same were purchased prior to 2009.

Petitioner also argues that the assessments have already prescribed. He said that the extraordinary prescription of 10 years under ***Section 222 of the Tax Code*** does not find application in this case since respondent failed to establish his guilt of fraud.

Finally, petitioner points out that he was denied of due process. He explains that the rushed issuance of the FLD deprived him of an opportunity to respond and to counter the findings in the PAN. He contends that the respondent merely replicated the PAN in issuing the FLD proving that he was not given an opportunity to be heard in a meaningful manner as required by jurisprudence.

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93 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 Taxpayer's Criminal Violation of the Code Through Payment of a Suggested Compromise Penalty, 6 September 1999.

Respondents' Counter-Arguments[94]

Respondent counters that the assessments are valid since these were issued pursuant to ***Section 6 of the Tax Code***. He explains that the ***Sony Case*** is inapplicable herein considering the existence of fraud, specifically, petitioner's failure to file his ITR for taxable years 2002 to 2006 and 2008 to 2009 and non-declaration of income in 2007 despite his continued purchase of luxury vehicles and capital investments in Villarica Country Homes and Marilao Coliseum.

He insists that the BIR was justified in extending the coverage of the LOA to "unverified prior years" since at the time of its issuance, it was still investigating when petitioner started his illegal acts. He argues that the fraudulent acts of petitioner necessitated the issuance of an LOA covering several taxable periods.

Respondent belies petitioner's argument that the assessments lack factual and legal bases. He stresses that the said issuances are based on vital information obtained by the BIR from a concerned citizen and third-party information sources (e.g. Securities and Exchange Commission, Land Transportation Office, and Local Government of Marilao, Bulacan). He argues that he was justified in using third-party information as basis of the assessments considering that the records of petitioner are manifestly inaccurate or incomplete.

He posits that the factual and legal bases of the assessments were explained in the Details of Discrepancy attached with the PAN and FLD. He points out that the Court is bound to uphold the validity of the assessments since they are presumed correct and made in good faith which petitioner failed to overturn.

Lastly, respondent contends that his right to assess petitioner has not prescribed. He explains that the applicable prescriptive period, in this case, is 10 years considering the existence of fraud on the part of petitioner, as provided under ***Section 222 of the Tax Code***.

The Ruling of the Court

After carefully reviewing the arguments made by both parties, the Court deems it proper to grant the Petition.

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[94] Respondent's Memorandum, Division Records Vol. 5, pp. 2217-2233.

<u>The LOA issued against Petitioner is valid only insofar as taxable year 2009 is concerned.</u>

As pointed out by the parties, the power of the CIR to authorize the examination and assessment of a taxpayer is found under ***Section 6 of the Tax Code***, 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 **<u>may authorize the examination of any taxpayer and the assessment of the correct amount of tax:</u>** Provided, however, That failure to file a return shall not prevent the Commissioner from **<u>authorizing the examination of any taxpayer.</u>** xxx (Emphasis and underscoring supplied)

The authority mentioned in the above-quoted provision is identified in ***Section 13 of the Tax Code*** as the LOA which is a "notice to the taxpayer that it is under investigation for possible deficiency tax assessment; at the same time it authorizes or empowers a designated revenue officer to examine, verify, and scrutinize a taxpayer's books and records, in relation to internal revenue tax liabilities for a particular period."[95]

The importance of the said instrument cannot be discounted considering that the CIR's authorized representatives may only proceed with the audit and assessment of a taxpayer if they are empowered pursuant to a valid LOA. The lack of the same will render the audit and assessment of the taxpayer void and ineffectual.[96]

In order to determine the validity of an LOA, the Supreme Court in numerous cases[97] has referred to ***RMO No. 43-90*** as the general guideline in the issuance of LOAs. Relevant to this case is the discussion on the allowable taxable periods to be covered by an LOA which reads, as follows:

> 3. A Letter of Authority **should cover a taxable period not exceeding one taxable year**. **<u>The practice of issuing L/As covering audit of "unverified prior years" is hereby prohibited. If the audit of a</u>**

[95] Commissioner of Internal Revenue v. Lancaster Philippines, Inc., G.R. No. 183408, 12 July 2017.

[96] AFP General Insurance Corp. v. Commissioner of Internal Revenue, G.R. No. 222133, 4 November 2020.

[97] Commissioner of Internal Revenue v. Lancaster Philippines, Inc., G.R. No. 183408, 12 July 2017; (Commissioner of Internal Revenue v. De La Salle University, Inc., G.R. Nos. 196596, 198841 & 198941, 9 November 2016.

> **taxpayer shall include more than one taxable period, the other periods or years shall be specifically indicated in the L/A.**
> (Emphasis and underscoring supplied)

Another applicable issuance is ***RMO No. 27-10,***[98] which prescribes the policies in the issuance of LOAs for audit investigations under the jurisdiction of the NID. The discussion pertinent to the issue is hereby quoted, to wit:

> "The issuance of LAs shall **cover only the taxable year(s) for which prima facie evidence of tax fraud, or of violations of the Tax Code, was established through the appropriate preliminary investigation**, unless the **investigation of prior or subsequent years is necessary** in order to:
>
> - Determine or trace continuing transactions entered into in the covered year and concluded thereafter, or those transactions concluded in the covered year that were commenced in prior years; or
> - Establish that the same scheme was utilized for prior or subsequent years."
>
> (Emphasis and underscoring supplied).

In harmonizing both legal pronouncements, it is clear that they do not prohibit the issuance of an LOA covering more than one taxable period. More so in audits conducted by the NID when the investigation of prior or subsequent years is necessary in order to determine the transactions or scheme employed by the taxpayer in not paying the correct taxes. However, what the guidelines prohibit is the issuance of LOAs covering "unverified prior years."

The foregoing prohibition is founded on the taxpayer's right to due process, as discussed by the Supreme Court in the case of ***CIR v. De La Salle University, Inc., (hereinafter referred to as "DLSU Case"),***[99] which was promulgated after the ***Sony Case*** to wit:

> "**What this provision clearly prohibits is the practice of issuing LOAs covering audit of unverified prior years.** RMO 43-90 does not say that a LOA which contains unverified prior years is void. It merely prescribes that if the audit includes more than one taxable period, **the other periods or years must be specified. The provision read as a whole requires that if a taxpayer is audited for more than one taxable year, the BIR must specify each taxable year or taxable period on separate LOAs.**
>
> **Read in this light, the requirement to specify the taxable period covered by the LOA is simply to inform the taxpayer of the extent of the audit and the scope of the revenue officer's authority. Without this**

[98] Re-invigorating the Run After Tax Evaders (RATE) Program, and Amending Certain Portions of RMO No. 24-2008, 15 March 2010.

[99] G.R. Nos. 196596, 198841 & 198941, 9 November 2016.

> **<u>rule, a revenue officer can unduly burden the taxpayer by demanding random accounting records from random unverified years, which may include documents from as far back as ten years in cases of fraud audit</u>.**"
> (Emphasis and underscoring supplied)

Jurisprudence has also clarified that in the event an LOA is issued covering a specific taxable year and "unverified prior years", the LOA will not be rendered void in its entirety but will be valid as to the declared taxable year. Relevant to this is the case of ***CIR v. Gaw, Jr., (hereinafter referred to as "Gaw Case")***,[100] to wit:

> "**It is settled that when a LOA authorizes an examination for a taxable year and "unverified prior years," in contravention of Revenue Memorandum Order No. 43-90, <u>it is not void in its entirety and shall be valid as to the declared taxable year</u>.** It is for this reason that the CTA First Division correctly limited its disposition to the cancellation of the deficiency income tax assessment for taxable year 2007 amounting to P1,295,855,151.89, as found in FDDA No. 2012-0001."
> (Emphasis and underscoring supplied)

In this case, the LOA issued against petitioner authorizing the audit investigation of his books of accounts and other accounting records covered not only Calendar Year 2009 but also "unverified prior years." The pertinent portion of the LOA[101] is hereby quoted, to wit:

> "The bearer(s) hereof ROs A.M. Simpit, L. Sante, G. Saga & G. Eito Under the supervision of Aurora V. Flor, of the National Investigation Division is/are authorized to examine your books of accounts and other accounting records for All Internal Revenue Taxes for **<u>the period from Calendar Year 2009 and unverified prior years.</u>** He is/ They are provided with the necessary identification card(s) which shall be presented to you upon request."
> (Emphasis and underscoring supplied)

Adopting the doctrine in the ***DLSU Case and Gaw Case***, the Court rules that the LOA issued to petitioner is valid only in so far as taxable year 2009 is concerned. Meanwhile, the "unverified prior years" which corresponds to taxable years 1998, 2000, 2001, 2006, 2007, and 2008 and the resulting assessments therefrom are void since these periods were not specifically indicated in the LOA as required by ***RMO No. 43-90*** and jurisprudence.

Unfortunately for respondent, his argument that the BIR was justified in issuing the LOA covering "unverified prior years" since it was still investigating when petitioner started his illegal acts is insufficient justification to side-step the strict implementation of ***RMO No. 43-90***. As discussed above, *ℓ*

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[100] G.R. No. 248070, 1 October 2019.
[101] Exhibit "R-24", Division Records Vol. 5, p. 2197; Exhibit "P-15", Division Records Vol. 3, p. 1396.

indicating the specific covered taxable periods in the LOA is anchored on the taxpayer's rights to due process which the BIR is duty-bound not to ignore.

Notwithstanding the foregoing finding that the LOA is valid at least for taxable year 2009, the Court is nonetheless constrained to declare the resulting assessments void on the ground that the same were issued in violation of petitioner's right to due process, as threshed out below.

The assessments were issued in violation of petitioner's right to due process rendering the same void.

Petitioner invokes the findings in the ***CTA Criminal Case*** where the Court of Tax Appeals found the subject assessments void for failure of the BIR to afford him due process in the issuance of the FLD and assessment notices.

In the ***CTA Criminal Case***, the Court was able to verify, based on the registry return card, that petitioner only received the PAN on 13 June 2011 or three (3) days before the FLD was issued on 16 June 2011. On this note, the CTA concluded that the BIR violated petitioner's right to due process.

Inopportunely, the Court cannot refer to the ***CTA Criminal Case*** in resolving the validity of the assessments in this case since petitioner neither presented nor offered the contended Decision or the registry return card of the PAN as part of his evidence.

Likewise, this Court is precluded from taking judicial notice of the said Decision since it was decided by a coordinate court, as discussed in the case of ***T'boli Agro-Industrial Development Inc., ("TADI") v. Solilapsi***,[102] to wit:

> "Respondent also claims that he could not have concealed the pendency of Civil Case Nos. 179 and 180 since all the cases were filed before the same MCTC presided over by Judge Sollesta, who should have taken judicial notice of such cases. This contention is erroneous. As a general rule, **courts are not authorized to take judicial notice in the adjudication of cases pending before them of the contents of other cases even when such cases have been tried or are pending in the same court and notwithstanding the fact that both cases may have been tried or are actually pending before the same judge. Courts may be required to take judicial notice of the decisions of the appellate courts but not of the decisions of the coordinate trial courts, or even of a decision or the facts involved in another case tried by the same court itself, unless the parties introduce the same in evidence or the court, as a matter of convenience, decides to do so.** Besides, judicial notice of matters which ought to be

[102] A.C. No. 4766, 27 December 2002.

known to judges because of their judicial functions is only discretionary upon the court. It is not mandatory.
(Emphasis and underscoring supplied)

On this note, the Court is compelled to resolve the issue regarding the assessments' validity based on the evidence presented by the parties herein.

In ***Montoya v. Varilla***,[103] the Supreme Court elucidated that the essence of due process in administrative proceedings is the opportunity given to a party to be heard, explain his/her side, and an opportunity to seek reconsideration of an action or ruling against him/her, to wit:

> "Though procedural rules in administrative proceedings are less stringent and often applied more liberally, **administrative proceedings are not exempt from basic and fundamental procedural principles, such as the right to due process in investigations and hearings.** The right to substantive and procedural due process is applicable to administrative proceedings.
>
> **Well-settled is the rule that the essence of due process is simply an opportunity to be heard or, as applied to administrative proceedings, an opportunity to explain one's side or an opportunity to seek a reconsideration of the action or ruling complained of**. Unarguably, this rule, as it is stated, **strips down administrative due process to its most fundamental nature and sufficiently justifies freeing administrative proceedings from the rigidity of procedural requirements**. In particular, however, due process in administrative proceedings has also been recognized to include the following: (1) the right to actual or constructive notice of the institution of proceedings which may affect a respondent's legal rights; (2) **a real opportunity to be heard personally or with the assistance of counsel**, to present witnesses and evidence in one's favor, and to defend one's rights; (3) a tribunal vested with competent jurisdiction and so constituted as to afford a person charged administratively a reasonable guarantee of honesty as well as impartiality; and (4) a finding by said tribunal which is supported by substantial evidence submitted for consideration during the hearing or contained in the records or made known to the parties affected."
> (Emphasis and underscoring supplied)

Relatively, the BIR is bound to follow ***RR No. 12-99*** which prescribes the due process requirement in the issuance of assessments to taxpayers. The relevant portion of the provision is hereby quoted, to wit:

> "SECTION 3. Due Process Requirement in the Issuance of a Deficiency Tax Assessment. —
>
> 3.1 Mode of procedures in the issuance of a deficiency tax assessment:

103 G.R. No. 180146, 18 December 2008.

xxx xxx xxx

3.1.2 Preliminary Assessment Notice (PAN). — If after review and evaluation by the Assessment Division or 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 for any deficiency tax or taxes, the said Office shall issue to the taxpayer, at least by registered mail, a Preliminary Assessment Notice (PAN) for the proposed assessment, showing 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). **If the taxpayer fails to respond within fifteen (15) days from date of receipt of the PAN, he shall be considered in default, in which case, a formal letter of demand and assessment notice shall be caused to be issued by the said Office, calling for payment of the taxpayer's deficiency tax liability, inclusive of the applicable penalties.**

xxx xxx xxx

3.1.4 Formal Letter of Demand and Assessment Notice. — The formal letter of demand and assessment notice shall be issued by the Commissioner or his duly authorized representative. The letter of demand 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 formal letter of demand and assessment notice shall be void (see illustration in ANNEX B hereof). The same shall be sent to the taxpayer only by registered mail or by personal delivery. If sent by personal delivery, the taxpayer or his duly authorized representative shall acknowledge receipt thereof in the duplicate copy of the letter of demand, showing the following: (a) His name; (b) signature; (c) designation and authority to act for and in behalf of the taxpayer, if acknowledged received by a person other than the taxpayer himself; and (d) date of receipt thereof."
(Emphasis and underscoring supplied)

As can be gleaned above, part of the due process requirement in issuing the FLD is giving the taxpayer 15 days from his/her receipt of the PAN to file his/her protest thereto. It is only after receiving the taxpayer's response, or the lapse of the 15-day period, that the BIR can issue the FLD and the corresponding assessment notice to the taxpayer.

Failure to strictly comply with this requirement will render the corresponding assessment void,[104] as stressed in ***Commissioner of Internal Revenue v. Yumex Philippines Corp.***,[105] citing ***Commissioner of Internal Revenue v. Avon Products Manufacturing, Inc.***,[106] ***Commissioner of Internal Revenue v. Metro Star Superama, Inc.***,[107] and ***Pilipinas Shell Petroleum Corp. v. Commissioner of Internal Revenue***,[108] to wit:

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104 Commissioner of Internal Revenue v. Pacific Bayview Properties, Inc., C.T.A. EB Case No. 1677, 8 October 2018.
105 G.R. No. 222476, 5 May 2021.
106 G.R. Nos. 201398-99 & 201418-19, 3 October 2018.
107 G.R. No. 185371, 8 December 2010.
108 G.R. No. 172598, 21 December 2007.

"Clearly from the aforequoted provisions, the taxpayer has fifteen (15) days from date of receipt of the PAN to respond to the said notice. <u>Only after receiving the taxpayer's response or in case of the taxpayer's default can respondent issue the FLD/FAN,</u>

Per the evidence on record, the BIR issued a PAN dated December 16, 2010, which it posted by registered mail the next day, December 17, 2010. It then issued and mailed the FLD/FAN on January 10, 2011. Although posted on different dates, the PAN and FLD/FAN were both received by the Post Office of Dasmariñas, Cavite, on January 17, 2011, and served upon and received by respondent on January 18, 2011. Under the circumstances, respondent was not given any notice of the preliminary assessment at all and was deprived of the opportunity to respond to the same before being given the final assessment.

In Commissioner of Internal Revenue v. Avon Products Manufacturing, Inc. (Avon case), **<u>the Court enjoined strict observance by the BIR of the prescribed procedure for issuance of the assessment notices with due regard for the taxpayers' constitutional rights</u>**. It is mandatory that the BIR not only inform the taxpayer through the PAN, FLD, and FAN of the facts, law and regulations, and jurisprudence on which the assessment against it is based, **but it must also accord the taxpayer the opportunity to be heard through the entire process**, i.e., from tax investigation until tax assessment. Pertinent portions of the Avon Case are reproduced below:

> The Bureau of Internal Revenue is the primary agency tasked to assess and collect proper taxes, and to administer and enforce the Tax Code. To perform its functions of tax assessment and collection properly, it is given ample powers under the Tax Code, such as the power to examine tax returns and books of accounts, to issue a subpoena, and to assess based on best evidence obtainable, among others. However, these powers must "be exercised reasonably and [under] the prescribed procedure." The Commissioner and revenue officers must strictly comply with the requirements of the law, with the Bureau of Internal Revenue's own rules, and with due regard to taxpayers' constitutional rights.
>
> xxx xxx xxx
>
> The importance of providing the taxpayer with adequate written notice of his or her tax liability is undeniable. Under Section 228, it is explicitly required that the taxpayer be informed in writing of the law and of the facts on which the assessment is made; otherwise, the assessment shall be void. Section 3.1.2 of Revenue Regulations No. 12-99 requires the Preliminary Assessment Notice to show in detail the facts and law, rules and regulations, or jurisprudence on which the proposed assessment is based. Further, Section 3.1.4 requires that the Final Letter of Demand must state the facts and law on which it is based; otherwise, the Final Letter of Demand and Final Assessment Notices themselves shall be void. Finally, Section 3.1.6 specifically requires that the decision of the

> Commissioner or of his or her duly authorized representative on a disputed assessment shall state the facts and law, rules and regulations, or jurisprudence on which the decision is based. Failure to do so would invalidate the Final Decision on Disputed Assessment.
>
> "The use of the word 'shall' in Section 228 of the [National Internal Revenue Code] and in [Revenue Regulations] No. 12-99 indicates that the requirement of informing the taxpayer of the legal and factual bases of the assessment and the decision made against him [or her] is mandatory." This is an essential requirement of due process and applies to the Preliminary Assessment Notice, Final Letter of Demand with the Final Assessment Notices, and the Final Decision on Disputed Assessment.
>
> On the other hand, the taxpayer is explicitly given the opportunity to explain or present his or her side throughout the process, from tax investigation through tax assessment. Under Section 3.1.1 of Revenue Regulations No. 12-99, the taxpayer is given 15 days from receipt of the Notice for Informal Conference to respond; otherwise, he or she will be considered in default and the case will be referred to the Assessment Division for appropriate review and issuance of deficiency tax assessment, if warranted. <u>**Again, under Section 228 of the Tax Code and Section 3.1.2 of Revenue Regulations No. 12-99, the taxpayer is required to respond within 15 days from receipt of the Preliminary Assessment Notice; otherwise, he or she will be considered in default and the Final Letter of Demand and Final Assessment Notices will be issued.**</u> After receipt of the Final Letter of Demand and Final Assessment Notices, the taxpayer is given 30 days to file a protest, and subsequently, to appeal his or her protest to the Court of Tax Appeals.

The Court, in Commissioner of Internal Revenue v. Metro Star Superama, Inc., stressed the importance of the PAN, in particular, as a substantive, and not just a formal, due process requirement, thus:

> **Indeed, Section 228 of the Tax Code clearly requires that the taxpayer must first be informed that he is liable for deficiency taxes through the sending of a PAN.** <u>**He must be informed of the facts and the law upon which the assessment is made. The law imposes a substantive, not merely a formal, requirement. To proceed heedlessly with tax collection without first establishing a valid assessment is evidently violative of the cardinal principle in administrative investigations — that taxpayers should be able to present their case and adduce supporting evidence.**</u>
>
> xxx xxx xxx
>
> From the provision quoted above, it is clear that the sending of a PAN to taxpayer to inform him of the assessment made is but part of the "due process requirement

in the issuance of a deficiency tax assessment," the absence of which renders nugatory any assessment made by the tax authorities. The use of the word "shall" in subsection 3.1.2 describes the mandatory nature of the service of a PAN. The persuasiveness of the right to due process reaches both substantial and procedural rights and the failure of the CIR to strictly comply with the requirements laid down by law and its own rules is a denial of Metro Star's right to due process. Thus, for its failure to send the PAN stating the facts and the law on which the assessment was made as required by Section 228 of R.A. No. 8424, the assessment made by the CIR is void.

xxx xxx xxx

It is an elementary rule enshrined in the 1987 Constitution that no person shall be deprived of property without due process of law. In balancing the scales between the power of the State to tax and its inherent right to prosecute perceived transgressors of the law on one side, and the constitutional rights of a citizen to due process of law and the equal protection of the laws on the other, the scales must tilt in favor of the individual, for a citizen's right is amply protected by the Bill of Rights under the Constitution. Thus, while "taxes are the lifeblood of the government," the power to tax has its limits, in spite of all its plenitude. Hence in Commissioner of Internal Revenue v. Algue, Inc., it was said —

> Taxes are the lifeblood of the government and so should be collected without unnecessary hindrance. On the other hand, such collection should be made in accordance with law as any arbitrariness will negate the very reason for government itself. It is therefore necessary to reconcile the apparently conflicting interests of the authorities and the taxpayers so that the real purpose of taxation, which is the promotion of the common good, may be achieved.
>
> xxx xxx xxx
>
> It is said that taxes are what we pay for civilized society. Without taxes, the government would be paralyzed for the lack of the motive power to activate and operate it. Hence, despite the natural reluctance to surrender part of one's hard-earned income to taxing authorities, every person who is able to must contribute his share in the running of the government. The government for its part is expected to respond in the form of tangible and intangible benefits intended to improve the lives of the people and enhance their moral and material values. This symbiotic relationship is the rationale of taxation and should dispel the erroneous notion that it is

> an arbitrary method of exaction by those in the seat of power.
>
> But even as we concede the inevitability and indispensability of taxation, it is a requirement in all democratic regimes that it be exercised reasonably and in accordance with the prescribed procedure. If it is not, then the taxpayer has a right to complain and the courts will then come to his succor. For all the awesome power of the tax collector, he may still be stopped in his tracks if the taxpayer can demonstrate . . . that the law has not been observed.

That respondent was able to file a protest to the FLD/FAN is of no moment. In Pilipinas Shell Petroleum Corporation v. Commissioner of Internal Revenue, the BIR ignored RR No. 12-99 and did not issue to the taxpayer, Pilipinas Shell Petroleum Corporation (PSPC), a notice for informal conference and a PAN as required; and as a result, deprived PSPC of due process in contesting the formal assessment levied against it. The Court pronounced therein that **"[w]hile PSPC indeed protested the formal assessment, such does not denigrate the fact that it was deprived of statutory and procedural due process to contest the assessment before it was issued."** The Court once more reminded the BIR to be more circumspect in the exercise of its functions as the power of taxation is also sometimes called the power to destroy and, therefore, should be exercised with caution to minimize injury to the proprietary rights of the taxpayer."
(Emphasis and underscoring supplied)

Here, petitioner stated in his Petition for Review[109] and Amended Judicial Affidavit[110] that he received the PAN on 1 June 2011. The Court reproduces the relevant portions of both submissions, as follows:

"Statement of Facts

4.4 Subsequently, respondent Commissioner **<u>issued an undated Preliminary Assessment Notice ("PAN", for brevity) which was received by petitioner on 01 June 2011.</u>** The undated PAN covered "deficiency internal revenue taxes for taxable year 2009 & unverified prior years".

"AMENDED JUDICIAL AFFIDAVIT OF WILLIAM R. VILLARICA

10. QUESTION: Mr. Witness, what happened a few years after the closure of your pawnshop business?

ANSWER: **<u>I received an undated Preliminary Assessment Notice ("PAN", for brevity) on 01 June 2011 covering my alleged "deficiency internal revenue taxes for taxable year 2009 & unverified prior years.</u>**"
(Emphasis and underscoring supplied)

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109 Petition for Review, p. 4, Division Records, Vol. 1, p. 13.
110 Exhibit "P-22", p. 4, Division Records Vol. 2, p. 634.

The foregoing statements of petitioner are consistent with the assertion he made in his Reply to the Preliminary Assessment Notice[111] which he sent, via registered mail, on 16 June 2011, and received by respondent on 5 July 2011.[112] The relevant portion of the document is hereby reproduced, to wit:

> "**Mr. Villarica received a copy of the PAN on 01 June 2011.** Since he has fifteen (15) days from receipt of the PAN to contest the assessment, Mr. Villarica may submit the instant letter until 16 June 2011." (Emphasis and underscoring supplied)

Considering that petitioner received the PAN on 1 June 2011, he, therefore, had 15 days from the said date or until 16 June 2011 to file his Reply to the PAN. Similarly, respondent is prohibited by ***Section 3 of RR No. 12-99*** to issue the FLD and assessment notices until he receives petitioner's response to the PAN or, in case of default, the end of the 15-day period or until 16 June 2011.

Instead of observing the foregoing period requirements, respondent hastily issued the FLD and the assessment notices on 16 June 2011, as admitted by respondent's witness in her Judicial Affidavit[113] and during her cross-examination in open court held on 16 January 2020.[114] The relevant portion of her testimony is reproduced, as follows:

"JUDICIAL AFFIDAVIT OF
REVENUE OFFICER ANGELA MARIE S. DE LEON

54. Q. What was the action on your recommendation, if any?

    A. Our recommendation was approved. **Thus, a Formal Letter of Demand dated June 16, 2011, together with the Details of Discrepancies and Audit Result/Assessment Notices, were issued to and served to petitioner**.

xxx xxx xxx

"TRANSCRIPT

ATTY. TUMBALI

Q. **On the Formal Letter of Demand, however, R-34, there is a date June 16, 2011, correct**?

[111] Exhibit "P-3", p. 1, Division Records Vol. 3, p. 1274.
[112] Reply to the Preliminary Assessment Notice, BIR Records No. 7, p. 978.
[113] Exhibit "R-40", Division Records Vol. 4, p. 1542.
[114] TSN dated 16 January 2020, pp. 21-21.

REVENUE OFFICER DE LEON

A. Yes, sir.

ATTY. TUMBALI

Q. Now, Ms. Witness, what is the **significance of this date, the June 16, 2011**?

REVENUE OFFICER DE LEON

A. **The date we made the Formal Letter of Demand**.

ATTY. TUMBALI

Q. So it is the **date of preparation**?

REVENUE OFFICER DE LEON

A. **Yes, sir**.

ATTY. TUMBALI

Q. So you mean to say that the Formal Letter of Demand was prepared as early as June 16, 2011, correct?

REVENUE OFFICER DE LEON

A. Can you repeat the question?

ATTY. TUMBALI

Q. That the Formal Letter of Demand was prepared as early as June 16, 2011?

REVENUE OFFICER DE LEON

A. **No, sir. It was on June 16.**

ATTY. TUMBALI

Q. **Okay. So it was prepared on that specific date?**

REVENUE OFFICER DE LEON

A. **Yes, sir**."
(Emphasis and underscoring supplied)

Clearly, the FLD and assessment notices were issued without waiting for the lapse of the mandatory 15-day period or his receipt of petitioner's Reply to the Preliminary Assessment Notice. This action by respondent disregarded the mandatory due process requirement laid down under ***Section 3 of RR No. 12-99***, as ruled in ***Commissioner of Internal Revenue v. Nippo Metal Tech Phils., Inc.***,[115] to wit:

> "In this case, the records show that respondent received the PAN on February 5, 2009. **However, without waiting for the lapse of the 15-day period, the CIR already issued the FLD/FAN. By disregarding the 15-day period provided by law, the CIR utterly deprived respondent of the opportunity to contest the PAN and present evidence in support thereto before an FLD/FAN was issued**.
>
> In CIR v. Metro Star Superama, Inc., **the Court emphasized that the PAN is part of due process. The persuasiveness of the right to due process reaches both substantial and procedural rights and the failure of the CIR to strictly comply with the requirements laid down by law and its own rules, as in this case, is a denial of the taxpayer's right to due process.**"
> (Emphasis and underscoring supplied)

Consequently, in view of respondent's violation of petitioner's right to due process, the Court is constrained to declare the assessments void and without legal effect.

The assessments are void for lack of factual and legal bases.

Aside from the foregoing discussions, the assessments must be struck down for lack of factual and legal bases.

It has been shown that respondent assessed petitioner for income tax and VAT on the basis of his alleged purchases and investments made during taxable years 1998, 2000, 2001, 2006, 2007, 2008, and 2009. He opines that these purchases and investments prove that petitioner has "unaccounted source of cash" which he failed to declare for income tax and VAT purposes.

However, a perusal of the assessments demonstrates that respondent failed to prove that this unaccounted source of cash is tantamount to income, and/or receipts/sales received by petitioner during the contested taxable periods.

[115] G.R. No. 227616, 19 June 2019.

In ***Bureau of Internal Revenue v. First E-Bank Tower Condominium Corp.***,[116] the Supreme Court declared Gross Income as "income derived from whatever source, including compensation for services; the conduct of trade or business or the exercise of a profession; dealings in property; interests; rents; royalties; dividends; annuities; prizes and winnings; pensions; and a partner's distributive share in the net income of a general professional partnership, among others."

Meanwhile, in ***Commissioner of Internal Revenue v. Court of Appeals***,[117] the High Court discussed three elements before a transaction can be subjected to income tax, to wit:

> "The **three elements in the imposition of income tax** are: **<u>(1) there must be gain or profit, (2) that the gain or profit is realized or received, actually or constructively, and (3) it is not exempted by law or treaty from income tax</u>**. Any business purpose as to why or how the income was earned by the taxpayer is not a requirement. **<u>Income tax is assessed on income received from any property, activity or service that produces the income</u>** because the Tax Code stands as an indifferent neutral party on the matter of where income comes from."
> (Emphasis and underscoring supplied)

As for the imposition of VAT, ***Section 105 of the Tax Code*** provides for instances on when a taxpayer may be held liable for the said tax, to wit:

> "SEC. 105. Persons Liable. - **Any person who, in the course of trade or business, sells barters, exchanges, leases goods or properties, renders services, and any person who imports goods shall be subject to the value-added tax (VAT) imposed in Sections 106 to 108 of this Code**.
>
> The value-added tax is an indirect tax and the amount of tax may be shifted or passed on to the buyer, transferee or lessee of the goods, properties or services. This rule shall likewise apply to existing contracts of sale or lease of goods, properties or services at the time of the effectivity of Republic Act No. 7716.
>
> The phrase "in the course of trade or business" means the regular conduct or pursuit of a commercial or an economic activity, including transactions incidental thereto, by any person regardless of whether or not the person engaged therein is a non-stock, nonprofit private organization (irrespective of the disposition of its net income and whether or not it sells exclusively to members or their guests), or government entity.
>
> The rule of regularity, to the contrary notwithstanding, services as defined in this Code rendered in the Philippines by nonresident foreign persons shall be considered as being rendered in the course of trade or business."
> (Emphasis and underscoring supplied)

[116] G.R. Nos. 215801 & 218924, 15 January 2020.
[117] G.R. No. 108576, 20 January 1999.

Hence, to be liable for VAT, there must be proof that the taxpayer, in the course of its trade or business, sold, bartered, leased, or rendered services in consideration of money or its equivalent. As for income tax, it is vital for the BIR to establish that the taxpayer received income from any property, activity or service. These rules are consistent with the findings of the CTA *En Banc* in ***Commissioner of Internal Revenue v. Philippine Power MC Distribution, Inc.***,[118] to wit:

> "Be that as it may, the alleged discrepancy/under-declared purchase cannot constitute an undeclared income. Consequently, the assessments for deficiency income tax should be cancelled.
>
> Three elements are necessary to impose income tax, namely: (a) there must be gain or profit, (b) the gain or profit is realized or received, actually or constructively, and (c) it is not exempted by law or treaty. **Therefore, income tax is assessed on income, which is received from any property, activity or service and must be clearly established that the taxpayer received such income.** This is clearly absent in this case. **The CIR failed to establish by clear and convincing evidence other than his alleged under-declared purchases on the part of PPMDI that the latter received an income that it did not declare in its return**.
>
> **The same is true for value-added tax (VAT), which is based either on the gross selling price or gross value in money of the goods or properties sold, bartered or exchanged, or gross receipts derived from the sale or exchange of services.**
>
> xxx xxx xxx
>
> **In assessing VAT, it must be shown that the taxpayer received an amount of money or its equivalent from its sale, barter or exchange of goods or properties, or from the sale or exchange of services performed. VAT, like income tax, also cannot be assessed based on under-declared purchases, precisely because no sale, exchange or gross receipt is involved. As correctly ruled upon by the former Second Division, VAT is imposed when one sells, not when one purchases.**
> (Emphasis and underscoring supplied)

In the instant case, the assessments were based on petitioner's alleged purchases of luxury vehicles, and investments in Villarica Country Homes and Marilao Coliseum. However, none of these transactions represent a sale, exchange, or gross receipts which can be subject to VAT. Neither was there any showing of income derived from these alleged purchases which can be subject to income tax.

Moreover, as for taxable year 2009, the Court cannot ascertain the factual basis of the income tax and VAT assessments since the tax base used does not correspond with the evidence on record. A reading of the PAN and

[118] C.T.A. EB Case No. 1940, 16 October 2019.

FLD shows that respondent assessed petitioner for deficiency taxes on account of improvements made to the Marilao Coliseum amounting to ₱7,006,628.00. However, the evidence presented by respondent in relation to the same is a Business Permit which reflects a capital investment of only ₱500,000.00 with 0 gross sales for 2009.

Given the foregoing, the Court finds that the assessments issued by respondent have no factual and legal foundation. The same are merely based on his presumption that the said unaccounted source of cash is tantamount to receipts/sales and income. Being a mere presumption, the assessments should be cancelled, in line with the landmark case of ***Collector of Internal Revenue v. Benipayo***,[119] to wit:

> "To our mind, the appealed decision **has no factual basis and must be reversed**. An assessment fixes and determines the tax liability of a taxpayer. As soon as it is served, an obligation arises on the part of the taxpayer concerned to pay the amount assessed and demanded. **Hence, assessments should not be based on mere presumptions no matter how reasonable or logical said presumptions may be**. Assuming arguendo that the average ratio of adults and children patronizing the Lucena Theater from 1949 to 1951 was 3 to 1, the same does not give rise to the inference that the same conditions existed during the years in question (1952 and 1953). The fact that almost that same ratio existed during the month of July, 1955 does not provide a sufficient inference on the conditions in 1952 and 1953.
> . . .
>
> **In order to stand the test of judicial scrutiny, the assessment must be based on actual facts. The presumption of correctness of assessment being a mere presumption cannot be made to rest on another presumption that the circumstances** in 1952 and 1953 are presumed to be the same as those existing in 1949 to 1951 and July 1955. **In the case under consideration there are no substantial facts to support the assessment in question**. . . ."
> (Emphasis and underscoring supplied)

The Court stresses that although "[t]axes are the lifeblood of the government and so should be collected without unnecessary hindrance.... such collection should be made in accordance with law as any arbitrariness will negate the very reason for government itself."[120] Considering the same, the Court has no other option but to strike down the assessments for being issued in violation of petitioner's rights to due process.

Having found the assessments void, the Court will no longer discuss the other issues raised in the present Petition.

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[119] G.R. No. L-13656, 31 January 1962 (cited in the case of Spouses Pacquiao v. Court of Tax Appeals, G.R. No. 213394, 6 April 2016.

[120] Commissioner of Internal Revenue v. BASF Coating + Inks Phils., Inc., G.R. No. 198677, 26 November 2014

WHEREFORE, premises considered, petitioner's Petition for Review is hereby **GRANTED**.

Accordingly, the Final Decision on Disputed Assessment, dated 4 April 2016, and the corresponding assessments issued against petitioner assessing him for deficiency income tax and VAT, inclusive of interest and surcharge, for taxable years 1998, 2000, 2001, 2006, 2007, 2008, and 2009 in the aggregate amount of ₱112,105,286.68 are hereby **CANCELLED** and **SET ASIDE**.

Consequently, respondent is hereby **ENJOINED** and **PROHIBITED** from proceeding with the collection of the assailed deficiency taxes assessed against petitioner.

SO ORDERED.

MARIA ROWENA MODESTO-SAN PEDRO
Associate Justice

WE CONCUR:

ERLINDA P. UY
Associate Justice

Ma. Belen

MA. BELEN M. RINGPIS-LIBAN
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

ERLINDA P. UY
Associate Justice
Chairperson

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.

ROMAN G. DEL ROSARIO
Presiding Justice