REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

THIRD DIVISION

HEAVENLY URBAN CHEF, INC.,
Petitioner,

-versus-

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

CTA Case No. 8556

Members:
BAUTISTA, Chairperson
FABON-VICTORINO, *and*
RINGPIS-LIBAN, *JJ.*

Promulgated:

AUG 09 2016
11:20 a.m.

x---x

DECISION

RINGPIS-LIBAN, *J.*:

Before this Court is a Petition for Review[1] filed by Heavenly Urban Chef, Inc. on October 12, 2012, praying that judgment be rendered ordering the Commissioner of Internal Revenue to abate its deficiency income tax, value-added tax (VAT), and improperly accumulated earnings tax (IAET) in the aggregate amount of ₱38,993,513.65, for taxable year 2009, broken down as follows:

	Basic	Interest	Surcharge	Total
Income Tax	₱ 5,638,563.46	₱ 2,848,633.16	₱ 2,819,281.73	₱ 11,306,478.35
Value-added Tax	13,182,288.55	7,237,618.16	6,591,144.28	27,011,050.99
Improperly Accumulated Earnings Tax	329,022.90	182,449.96	164,511.45	675,984.31
Total	**₱19,149,874.91**	**₱10,268,701.28**	**₱9,574,937.46**	**₱38,993,513.65**

[1] Docket, vol. I, pp. 6-18.

THE PARTIES

Petitioner Heavenly Urban Chef, Inc. is a domestic corporation duly organized and existing under the laws of the Philippines, with address at Lot 86 Bagsakan Road corner Avocado Street, FTI Complex, Taguig City.[2]

On the other hand, respondent is the Commissioner of the Bureau of Internal Revenue (BIR), vested by law with authority to decide, approve, and reverse assessments of internal revenue taxes. She holds office at the BIR National Office Building, Agham Road, Diliman, Quezon City.

THE FACTS

On January 18, 2010, Mission Order No. MSO200100076311[3] was issued by Regional Director Jaime B. Santiago, directing Revenue Officers Jefferson T. Ocampo, Ernesto P. Vibar, and Rafaelito C. Elias to monitor sales and/or place of business establishment of petitioner under observation or surveillance for violations of bookkeeping rules and regulations, particularly on non-issuance of receipts, and to apprehend violators of revenue laws and regulations, from January 18 to February 5, 2010.

On June 25, 2010, Letter of Authority No. 200700028216 was issued by Regional Director Santiago, authorizing Revenue Officers Jefferson T. Ocampo, Ernesto P. Vibar, and Rafaelito C. Elias, and Group Supervisor Rosalina C. Orcullo to examine petitioner's books of accounts and other accounting records for all internal revenue taxes for the period covering January 1, 2009 to December 31, 2009.[4]

On July 2, 2010, petitioner received a Notice for Presentation of Books of Accounts from respondent dated July 1, 2010, requesting the presentation of certain documents pursuant to the provision of Section 20 of Revenue Regulations (RR) No. V-1.[5] On July 21, 2010 and on August 10, 2010, respondent issued a Second Notice for Presentation of Books of Accounts[6] and a Final Request for Presentation of Records Re: Letter of Authority No. 00028216 dated June 25, 2010[7], respectively.

[2] Par. 2.01, The Parties, Petition for Review, docket, vol. I, p. 7; Par. 1, Stipulation of Facts, Joint Stipulation of Facts and Issues (JSFI), docket, vol., III, p. 1565; Par. 1, Facts, Pre-Trial Order, docket, vol. III, p. 1599.
[3] Exhibit "R-4", BIR Records, p. 4.
[4] Exhibit "R-6", BIR Records, p. 172.
[5] Exhibits "R-7" and "R-7-b", BIR Records, pp. 173-174.
[6] Exhibit "R-8", BIR Records, p. 176.
[7] Exhibit "R-9", BIR Records, p. 178.

For petitioner's failure to submit all requested documents, Revenue Officer Jefferson T. Ocampo served a Subpoena Duces Tecum addressed to Jean Paul Escudero, in his capacity as President of petitioner, dated September 3, 2010.[8]

Thereafter, on November 4, 2010, respondent filed a criminal complaint with the Prosecution Office of Makati City, against the officers of petitioner for alleged violation of Sections 5(C), 256, and 266 of the National Internal Revenue Code (NIRC) of 1997, as amended.[9]

A Notice for an Informal Conference[10] was issued by respondent on July 22, 2011.

On September 19, 2011, respondent issued a Preliminary Assessment Notice[11] (PAN) with attached Details of Discrepancies against petitioner.[12]

On October 3, 2011, petitioner submitted a Letter of Protest to the Regional Director of BIR Region 8 in Makati City.[13] In support of its protest, petitioner submitted a letter to the BIR, including schedules and other documents, on October 13, 2011. On December 1, 2011, petitioner again wrote a letter to the BIR, submitting documents for the year 2009.[14]

Petitioner received the Formal Assessment Notice (FAN) with Details of Discrepancies[15] dated March 22, 2012 from respondent, assessing petitioner for alleged deficiency income tax, VAT, and IAET in the aggregate amount of ₱37,136,238.10, broken down as follows:

INCOME TAX		
Taxable income/(loss) per ITR		₱ 3,750,458.00
Add: Adjustments/disallowance		
Unsupported expenses – 50% rule	₱ 444,666.00	
Undeclared sales	14,695,017.86	
Overclaimed expenses	39,733.00	15,179,416.86
Taxable income per audit		18,929,874.86
Basic income tax due		5,678,962.46
Less: Tax paid per ITR		
Payment	40,399.00	
Creditable tax withheld	1,084,798.00	

[8] Exhibit "R-11", BIR Records, p. 260.
[9] Par. 8, Stipulation of Facts, JSFI, docket, vol. III, p. 1566; Exhibit "R-12", BIR Records, pp. 263-265.
[10] Exhibit "R-17", Amended, BIR Records, p. 305.
[11] Exhibit "P-4" (Exhibit "D").
[12] Pars. 2 and 3, Stipulation of Facts, JSFI, docket, vol. III, p. 1565.
[13] Par. 4, Stipulation of Facts, JSFI, docket, vol. III, p. 1565.
[14] Exhibit "P-15" (Exhibit "G").
[15] Exhibit "P-33" (Exhibit "H"); Par. 5, Stipulation of Facts, JSFI, docket, vol. III, p. 1565.

Total	1,125,197.00	
Less: Unsupported creditable tax withheld	1,084,798.00	40,399.00
Basic deficiency income tax		5,638,563.46
Add: 50% surcharge	2,819,281.73	
Interest (04/16/10 to 04/30/2012)	2,301,769.74	5,121,051.47
TOTAL AMOUNT DUE		**₱10,759,614.93**

VALUE-ADDED TAX		
Vatable sales per return		₱ 22,225,437.83
Add: Sales not subjected to VAT		89,433,742.28
Adjusted Vatable sales		111,659,180.11
Output tax		13,399,101.61
Less: Creditable input tax		
Claimed input taxes	₱2,606,964.98	
Less: Unsupported input taxes	2,606,964.98	-
VAT payable		13,399,101.61
Less: Tax paid per return		216,813.06
Basic deficiency value-added tax		13,182,288.55
Add: 50% surcharge	6,591,144.28	
Interest (01/26/10 to 04/30/2012)	5,959,116.75	12,550,261.03
TOTAL AMOUNT DUE		**₱25,732,549.58**

IMPROPERLY ACCUMULATED EARNINGS TAX		
Basic deficiency tax		₱329,022.90
Add: 50% surcharge	₱ 164,511.45	
Interest (01/16/10 to 04/30/2012)	150,539.24	315,050.69
TOTAL AMOUNT DUE		**₱ 644,073.59**

TOTAL DEFICIENCY TAXES		**₱37,136,238.10**

In a letter dated and filed on April 3, 2012, petitioner protested the FAN and requested a re-investigation of the assessment issued by respondent.[16]

In response to the protest, respondent issued her Final Decision on Disputed Assessment (FDDA)[17] dated September 7, 2012, which was received by petitioner on September 12, 2012[18], upholding the FAN but increasing the deficiency amount to ₱38,993,513.65, due to an increase in the accruing interest:

INCOME TAX		
Taxable income/(loss) per ITR		₱ 3,750,458.00
Add: Adjustments/disallowance		
Unsupported expenses – 50% rule	₱ 444,666.00	
Undeclared sales	14,695,017.86	

[16] Exhibit "P-34" (Exhibit "I").
[17] Exhibit "P-35" (Exhibit "J").
[18] Par. 9, Stipulation of Facts, JSFI, docket, vol. III, p. 1566.

Overclaimed expenses	39,733.00	15,179,416.86
Taxable income per audit		18,929,874.86
Basic income tax due		5,678,962.46
Less: Tax paid per ITR		
Payment	40,399.00	
Creditable tax withheld	1,084,798.00	
Total	1,125,197.00	
Less: Unsupported creditable tax withheld	1,084,798.00	40,399.00
Basic deficiency income tax		5,638,563.46
Add: 50% surcharge	2,819,281.73	
Interest (04/16/10 to 10/24/2012)	2,848,633.16	5,667,914.89
TOTAL AMOUNT DUE		**₱11,306,478.35**

VALUE-ADDED TAX		
Vatable sales per return		₱ 22,225,437.83
Add: Sales not subjected to VAT		89,433,742.28
Adjusted Vatable sales		111,659,180.11
Output tax		13,399,101.61
Less: Creditable input tax		
Claimed input taxes	₱ 2,606,964.98	
Less: Unsupported input taxes	2,606,964.98	-
VAT payable		13,399,101.61
Less: Tax paid per return		216,813.06
Basic deficiency value-added tax		13,182,288.55
Add: 50% surcharge	6,591,144.28	
Interest (01/26/10 to 10/24/2012)	7,237,618.16	13,828,762.44
TOTAL AMOUNT DUE		**₱27,011,050.99**

IMPROPERLY ACCUMULATED EARNINGS TAX		
Basic deficiency tax		₱ 329,022.90
Add: 50% surcharge	₱ 164,511.45	
Interest (01/16/10 to 10/24/2012)	182,449.96	346,961.41
TOTAL AMOUNT DUE		**₱ 675,984.31**

TOTAL DEFICIENCY TAXES		**₱38,993,513.65**

Accordingly, petitioner filed the instant Petition for Review before this Court on October 12, 2012.[19]

In her Answer[20] filed on December 5, 2012, respondent interposed the following special and affirmative defenses:

> "6. She reiterates and repleads the preceding paragraphs of this answer as part of her Special and Affirmative Defenses;

[19] Docket, vol. I, pp. 6-18.

[20] Docket, vol. I, pp. 352-358.

7. The Final Decision on Disputed Assessment (FDDA) dated 7 September 2012 was issued by the respondent in reply to petitioner's Protest Letter dated April 3, 2012 against the Formal Assessment Notice (FAN) dated 22 March 2012;

8. Petitioner was assessed for deficiency income tax, value-added tax and improperly accumulated earnings tax for taxable year 2009, for the reason that during the administrative investigation of its tax case by the BIR, petitioner failed to substantiate or controvert by substantial evidence the BIR factual findings, as shown under the Details of Discrepancies attached to the Preliminary Assessment Notice (PAN) dated 19 September 2011, Formal Assessment Notice (FAN) dated 22 March 2012, as well as the Final Decision on Disputed Assessment (FDDA) dated 7 September 2012, which are briefly discussed hereunder, viz:

A. <u>On Income Tax:</u>

a. Petitioner failed to submit documents in support of its claimed deductions/expenses (i.e. Taxes and Licenses, Interest Expense, Light and Water, Supplies, Gasoline and Oil, Representation and Repairs and Maintenance) hence, the said expenses were disallowed as deduction from gross income pursuant to Section 34(A)(1) of the 1997 Tax Code. As such, since there is no means by which the correctness and accuracy of its expenses can be ascertained, 50% were disallowed following the ruling in the case of Mariano Zamora vs. Commissioner of Internal Revenue in relation to Section 2.4 of Revenue Memorandum Circular 23-2000, which states that 'if there is a showing that expenses have been incurred but the exact amount thereof cannot be ascertained due to absence of documentary evidence, it is the duty of the BIR to make an estimate of the deduction that may be allowable in computing the taxpayer's taxable income, bearing heavily against the taxpayer whose inexactitude is of his own making x x x'

b. Petitioner has an undeclared sales in the amount of P14,695,017.86 from July to December 2009 since after verification it was discovered that its business (Makati Branch) started its operation from July 2009 but per Integrated Tax System of the BIR it was only registered on March 24, 2010, hence, the taxable income of P14,695,017.86 was added to its gross income pursuant to Section 32 of the 1997 Tax Code.

c. Petitioner has an over-claimed expense in the amount of P39,733.00 since after verification it was disclosed that the total declared itemized deduction per ITR amounting to P17,230,841.00 exceeded the total deductions presented per Audited FS amounting to P17,191,108.00, hence, the amount of over-claimed expense were disallowed as deductions from gross income pursuant to Section 34(A)(1) of the 1997 Tax Code.

d. Petitioner failed to substantiate with sufficient evidence its claimed creditable withholding tax in the amount of P1,084,798.00, hence, the same were disallowed pursuant to Section 2.58.3(B) of Revenue Regulations No. 2-98, as amended.

B. <u>On Value-Added Tax:</u>

a. Petitioner failed to subject to VAT its sales amounting to P89,433,742.28 which was discovered after comparison of its sales per VAT return as against its sales per ITR, hence, such discrepancy was assessed pursuant to Section 106 of the 1997 Tax Code in relation to Revenue Regulations No. 16-2005, as amended.

b. Petitioner failed to submit the required VAT Invoice or Official Receipt to support its claimed input taxes in the amount of P2,606,964.98, hence, the same were disallowed in violation of Section 110(A)(1) of the 1997 Tax Code which states that 'Any input tax claimed evidenced by a VAT income or Official Receipt issued in accordance with Section 113 of the NIRC shall be creditable against output taxes.'

C. **On Improperly Accumulated Earnings Tax:**

a. Petitioner failed to withhold and remit the corresponding **Improperly Accumulated Earnings Tax** due amounting to P329,022.90, pursuant to Section 29 of the 1997 Tax Code in relation to Revenue Memorandum Circular No. 35-2011, as amended.

9. Respondent fully complied with the due process requirement mandated under Section 228 of the 1997 Tax Code, as implemented by Revenue Regulations No. 12-99, when the disputed Preliminary Assessment Notice (PAN) dated 19 September 2011, Formal Assessment Notice (FAN) dated 22 March 2012, as well as the Final Decision on Disputed Assessment (FDDA) dated 7 September 2012 were issued to herein petitioner. Records clearly show that petitioner was duly afforded an opportunity to controvert the factual findings of the respondent CIR involving its deficiency income tax, value-added tax and improperly accumulated earning tax for taxable year 2009 through the issuance of a Notice for Informal Conference, Preliminary Assessment Notice (PAN) dated 19 September 2011, Formal Assessment Notice (FAN) dated 22 March 2012, and Final Decision on Disputed Assessment (FDDA) dated 7 September 2012.

Likewise, petitioner was duly appraised by the respondent of the factual and legal basis on how and why he (respondent) arrived such a deficiency income tax, value-added tax and improperly accumulated earning tax for taxable year 2009 through the issuance of the Details of Discrepancies attached to the Formal Assessment Notice (FAN) dated 22 March 2012, Preliminary Assessment Notice (PAN) dated 19 September 2011, Notice for Informal Conference, as well as the Final Decision on Disputed Assessment (FDDA) dated 7 September 2012 and other

BIR Correspondence to petitioner which are found in the BIR records of this case.

10. This Honorable Court in the case of ***IDS LOGISTICS (PHILS.), INC., vs. CIR, C.T.A. CASE NO. 7540. May 20, 2010***, citing the ruling in **Bank of the Philippine Islands vs. Commissioner of Internal Revenue,** ***C.T.A. CASE No. 7397, April 9, 2008***, thoroughly discussed the ***due process rule in taxation***, as follows:

> 'Revenue Regulations No. 12-85 provides for the procedure covering the Administrative Protests on Assessments of the BIR. Under the said Revenue Regulation, a post-reporting notice is sent to the taxpayer for an informal conference when there are findings of deficiency taxes. Subsequent to this notice is the issuance of the pre-assessment notice upon findings of the Commissioner that an assessment for deficiency taxes should be issued. However, such pre-assessment notice may or may not be protested by the taxpayer. In fact, Section 5 of the same Revenue Regulation provides that 'In the event that the taxpayer fails to respond to the pre-assessment notice within the prescribed period... he should be informed of such fact and the report of investigation shall be given due course.'
>
> The essential elements of due process are notice and opportunity to present one's side. To begin with, petitioner had knowledge of the investigation being conducted by the BIR on its tax liabilities for the taxable years 1982-1986, as evidenced by the letter of respondent addressed to petitioner dated September 25, 1986 and received by petitioner on September 26, 1986. The said letter, in fact, requested for an informal conference on the matter and requested further that petitioner submits documentary evidence to support its stand.
>
> As the facts would demonstrate, ***petitioner was never deprived of due process as it was fully appraised of the legal and factual bases of the assessment issued against it; which enabled petitioner to substantially protest the arguments and issues raised. It is sufficient that there is notice to the taxpayer of the legal and factual***

> ***bases of the assessment; and to the Court, this is substantial compliance of what is mandated by Section 228 of the NIRC. Thus, so long as the parties are given the opportunity to explain their side, the requirements of due process are satisfactorily complied with.***' (Emphasis supplied)

11. The assessments issued against petitioner for deficiency income tax, value-added tax and improperly accumulated earning tax for taxable year 2009 were made pursuant to Section 6(B) of the 1997 Tax Code, which provides that 'when a report required by law as a basis for the assessment of any national internal revenue tax shall not be forthcoming within the time fixed by laws or rules and regulations or when there is a reason to believe that any such report is false, incomplete or erroneous, the Commissioner shall asses the proper tax on the best evidence obtainable.' And in relation to Revenue Memorandum Order No. 15-95, which provides that 'the failure to keep records or refusal to make certain records available for examination of the BIR is an indication of fraud.'

12. The failure of petitioner to present/submit its books of accounts and other accounting records for taxable year 2009 to the BIR during the administrative investigation of its tax case resulted to the issuance of the BIR Subpoena Duces Tecum dated 3 September 2010, and the consequent filing of the BIR of a criminal complaint against the responsible officers of petitioner for violation of the Sections 5(C), 256 and 266 of the 1997 Tax Code.

13. The assessments issued against petitioner for deficiency income tax, value-added tax and improperly accumulated earning tax for taxable year 2009 were made in accordance with law and regulations.

14. **Assessments are prima facie presumed correct and made in good faith, the taxpayer has the duty of proving otherwise. In the absence of proof of any irregularities in the performance of official duties, an assessment will not be disturbed. Hence, all presumptions are in favor of the correctness of the subject tax assessment issued by the respondent**. (*Interprovincial Autobus Co., Inc. vs. Collector of Internal Revenue, 98 Phil 290; Sy Po, vs. CTA, G.R. 81446, August 18, 1988; Dayrit vs. Cruz, L-39910, September 26, 1988; Cagayan Robina Sugar Milling Co., vs. CA, G.R. 122451, October 12, 2000*). **Failure to present proof of error in the assessment will justify judicial**

affirmation of said assessment (*Delta Motors Co., vs. CIR, CAT Case No. 3782, May 21, 1986; CIR vs. CA, G.R. Nos. 104151 and 105563, March 10, 1995*)."

The case was set for pre-trial conference on January 25, 2013.[21]

Respondent filed her Pre-Trial Brief[22] on January 16, 2013; while petitioner filed its Pre-Trial Brief[23] on January 22, 2013. However, upon motion of respondent,[24] the pre-trial conference was reset.[25]

On January 16, 2013, petitioner filed its Request for Admission by Adverse Party, requesting respondent to admit certain facts and documents pertinent to this case, pursuant to Rule 26 of the Rules of Court, as amended.

In a Comment filed on February 8, 2013, respondent admitted the following facts:

1. On September 19, 2011, petitioner received the Preliminary Assessment Notice (PAN) from the BIR RR8 Makati;

2. On October 3, 2011, petitioner submitted a Letter of Protest addressed to the Regional Director of the BIR;

3. On October 13, 2011, petitioner submitted a Letter to the BIR but denies the truthfulness of the attachments thereto;

4. On March 22, 2012, the BIR issued Formal Assessment Notices;

5. On April 3, 2012, petitioner submitted to the BIR a Letter dated April 3, 2012, received on April 25, 2012, protesting the Formal Assessment Notices (FAN) of the BIR; and

6. On September 12, 2012, petitioner received the denial in the Final Decision on Disputed Assessment (FDDA) issued by the BIR on September 7, 2012.

---

[21] Notice of Pre-Trial Conference, docket, vol. I, p. 360.
[22] Respondent's Pre-Trial Brief, docket, vol. I, pp. 362-365.
[23] Docket, vol. II, pp. 1046-1053.
[24] Manifestation with Urgent Ex-parte Motion to Reset Pre-trial Conference, docket, vol. I, pp. 372-373.
[25] Resolution dated January 25, 2013, docket, vol. II, p. 716.

The Court noted petitioner's Request for Admission by Adverse party and respondent's Comment thereto in a Resolution[26] dated March 14, 2013.

On August 1, 2013, the pre-trial conference was held.[27]

The parties filed their Joint Stipulation of Facts and Issues[28] on October 21, 2013, which was adopted by the Court in the Pre-Trial Order[29] dated December 10, 2013.

During trial, petitioner presented Mr. Arden Diano Retales,[30] its Finance Officer in the years 2010 to 2011, as its witness. Subsequently, petitioner formally offered its documentary evidence on August 12, 2014.[31]

The Court issued a Resolution[32] on September 10, 2014, admitting, as petitioner's evidence, Exhibits "P-1", "P-2", "P-3", "P-4", "P-5", "P-6", "P-7", "P-15", "P-24", "P-26", "P-29", "P-30", "P-31", "P-32", "P-33", "P-34", "P-35", "P-36", "P-37", "P-40", "P-41", "P-42", "P-43", "P-44", and "P-45". However, the Court denied the admission of Exhibits "P-8", "P-9", "P-12", "P-16", "P-22", and "P-25", for petitioner's failure to identify said exhibits; Exhibits "P-38" and "P-39", for petitioner's failure to present the originals for comparison; Exhibit "P-11", for not being found in the records of the case; Exhibits "P-13" and "P-14", for petitioner's failure to identify said exhibits and for not being found in the records; and Exhibit "P-10", for petitioner's failure to present the originals for comparison and failure to identify said exhibit.

On the other hand, respondent presented Revenue Officer Arturo D. Boniol, Jr.[33] and Revenue Officer Rosalina C. Orcullo.[34] Moreover, she filed her Formal Offer of Evidence[35] on May 7, 2015.

In a Resolution[36] dated May 27, 2015, the Court admitted Exhibits "R-1", "R-2", "R-2-A", "R-3", "R-3-A", "R-4", "R-4-A", "R-4-B", "R-5", "R-5-A", "R-6", "R-6-A", "R-6-B", "R-7", "R-7-A", "R-7-B", "R-8", "R-8-A", "R-8-B", "R-9", "R-9-A", "R-9-B", "R-10", "R-10-A", "R-11", "R-11-A", "R-11-B", "R-12", "R-12-A", "R-12-B", "R-13", "R-13-A", "R-14", "R-14-A", "R-15", "R-15-A", "R-15-B", "R-16", "R-16-A", "R-17", "R-17-A", "R-17-B", "R-18",

---

[26] Docket, vol. III, pp. 1423-1426.
[27] Minutes of the Hearing, docket, vol. III, p. 1541.
[28] Docket, vol. III, pp. 1565-1574.
[29] Docket, vol. III, pp. 1599-1610.
[30] Minutes of the Hearing dated January 23, 2014, docket, vol. III, p. 1620.
[31] Formal Offer of Evidence (For the Petitioner), docket, vol. III, pp. 1694-1706.
[32] Docket, vol. IV, pp. 1923-1924.
[33] Minutes of the Hearing, docket, vol. IV, p. 1950.
[34] Minutes of the Hearing, docket, vol. IV, p. 1956 and 1961.
[35] Docket, vol. IV, pp. 1977-1992.
[36] Docket, vol. IV, pp. 2003- 2004.

"R-18-A", "R-18-B", "R-18-C", "R-18-D", "R-19", "R-19-A", "R-20", "R-20-A", "R-21", "R-22", "R-21-A", "R-22-A", "R-23", "R-23-A", "R-24", "R-24-A", "R-25", "R-25-A", "R-26", "R-26-A", "R-27", "R-27-A", "R-27-B", "R-27-C", "R-27-D", "R-28", "R-28-A", "R-28-B", "R-28-C", "R-29", "R-30", "R-30-A", "R-31", and "R-31-A", as respondent's evidence.

As directed by the Court, petitioner filed its Memorandum[37] on August 3, 2015. Meanwhile, on July 16, 2015, respondent filed her Manifestation and Motion[38], stating that she is adopting the arguments found in the special and affirmative defenses of her Answer dated November 20, 2012, as part of her Memorandum, and praying that the Petition for Review be dismissed for lack of merit. Consequently, the case was declared submitted for decision on August 13, 2015.[39]

THE ISSUES

The parties submitted the following issues[40] for this Court's disposition:

1. Whether or not the assessment issued by respondent to petitioner for deficiency income in the total amount of ₱11,306,478.35 inclusive of tax surcharge and interest for taxable year 2009 has factual and legal bases;

2. Whether or not the assessment issued by respondent to petitioner for value-added tax in the total amount of ₱27,011,050.99 inclusive of tax surcharge and interest for taxable year 2009 has factual and legal bases;

3. Whether or not the assessment issued by respondent to petitioner for improperly accumulated earnings in the total amount of ₱675,984.31 inclusive of tax surcharge and interest for taxable year 2009 has factual and legal bases;

4. Whether or not the failure of petitioner to present/submit its books of accounts and other accounting records for taxable year 2009 to the BIR during the administrative investigation of its tax case which resulted in the issuance of the BIR Subpoena Duces Tecum dated September 3, 2010, and consequent filing of a criminal complaint against responsible officers of petitioner's corporation for violation of Section 5(C), 256, and 266 of the 1997 Tax Code justify the BIR-

[37] Memorandum and Manifestation, docket, vol. IV, pp. 2055-2078.
[38] Docket, vol. IV, pp. 2038-2040.
[39] Resolution dated August 13, 2015, docket, vol. IV, p. 2313.
[40] Stipulation of Issues, JSFI, docket, vol. III, pp. 1566-1567.

issued assessments based on the "Best Evidence Obtainable Rule" under Section 6(B) of the 1997 Tax Code.

The above-enumerated issues can be summarized into one main issue:

"Whether or not petitioner is liable for alleged deficiency income tax, VAT, and IAET in the respective amounts of ₱11,306,478.35, ₱27,011,050.99, and ₱675,984.31, including interest and surcharges, or in the aggregate amount of ₱38,993,513.65, for taxable year 2009."

PETITIONER'S ARGUMENTS

Petitioner insists that respondent has no legal basis to hold it liable for any additional taxes as all expenses incurred by it were fully substantiated and proved with supporting receipts. It also claims that it neither has undeclared sales nor unsupported creditable tax withheld contrary to respondent's ruling and assessment of additional income taxes.[41]

Furthermore, petitioner contends that the method used by respondent in determining the alleged undeclared sales was unsupported by any written testimony or report by any duly authorized personnel. Hence, it is speculative and the legal right of petitioner to due process was clearly violated by respondent's ruling.[42]

Moreover, petitioner avers that respondent erred when she deemed that its zero-rated transactions with VAT-registered corporate entities should have been subject to VAT. Petitioner also posits that contrary to respondent's position, it has no unsupported input taxes. In other words, respondent has no legal basis to hold it liable for any additional VAT.[43]

Finally, petitioner alleges that respondent committed serious error when she ruled that petitioner has improperly accumulated earnings resulting in deficiency taxes.[44]

RESPONDENT'S ARGUMENTS

Respondent, on the other hand, maintains that tax assessments made by tax examiners are presumed correct and made in good faith. She avers that the taxpayer has the duty of proving otherwise with strong and convincing

[41] Memorandum and Manifestation, docket, vol. IV, p. 2060.
[42] Memorandum and Manifestation, docket, vol. IV, p. 2061.
[43] Memorandum and Manifestation, docket, vol. IV, pp. 2074-2075.
[44] Memorandum and Manifestation, docket, vol. IV, p. 2075.

evidence and that in the absence of proof of any irregularities in the performance of official duties, the courts must not interfere or disturb such findings.[45]

Moreover, she claims that failure to present proof of error in the assessment will justify judicial affirmation of said assessment. According to respondent, since petitioner failed to prove by clear and convincing evidence that it is not liable to pay the assessed deficiency income tax, VAT, and improperly accumulated earnings tax for taxable year ending December 31, 2009, the presumption that the said deficiency tax assessment was made by respondent in accordance with law and regulations was not overcome by petitioner.[46]

THE RULING OF THE COURT

Jurisdiction of the Court of Tax Appeals

The Court of Tax Appeals is a court of special or limited jurisdiction and can only take cognizance of such matters as are clearly within its jurisdiction.[47] The jurisdiction of the CTA is conferred by Republic Act (RA) No. 1125, as amended by RA No. 9282. The provision pertinent to the instant case is quoted for ready reference:

> "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 or other laws administered by the Bureau of Internal Revenue; x x x" *(Emphasis supplied)*

[45] Manifestation and Motion, docket, vol. IV, pp. 2038-2039.
[46] Manifestation and Motion, docket, vol. IV, p. 2039.
[47] Allied Banking Corporation vs. Commissioner of Internal Revenue, G.R. No. 175097, February 5, 2010; Cathay Pacific Airways, Ltd. vs. Commissioner of Internal Revenue, CTA EB No. 717 (CTA Case No. 7876), April 17, 2012; Rizal Commercial Banking Corporation vs. Commissioner of Internal Revenue, G.R. No. 168498, Resolution dated April 24, 2007.

Moreover, Section 228 of the NIRC of 1997, as amended, provides that when a protest is denied in whole or in part, the taxpayer adversely affected by the decision may appeal to the CTA within thirty (30) days from receipt of said decision. Likewise, Section 3 of Rule 8 of the Revised Rules of the Court of Tax Appeals (RRCTA) provides the prescriptive period for filing a Petition for Review before the CTA, to wit:

> "SEC. 3. *Who may appeal; period to file petition.* – A party adversely affected by a decision, ruling or the inaction of the Commissioner of Internal Revenue on disputed assessments or claims for refund of internal revenue taxes, xxx may appeal to the Court by petition for review filed within thirty days after receipt of a copy of such decision or ruling, or expiration of the period fixed by law for the Commissioner of Internal Revenue to act on the disputed assessments. xxx"

Based on the foregoing provisions, the CTA has the power to determine whether or not petitioner is liable for deficiency income tax, VAT, and improperly accumulated earnings tax for taxable year 2009. Furthermore, since the Petition for Review was filed on October 12, 2012, or within 30 days from petitioner's receipt of the FDDA on September 12, 2012, the instant petition was timely filed. Hence, the Court has jurisdiction over the present case.

The Court shall now determine whether petitioner is liable for the deficiency taxes assessed by respondent.

I. Deficiency Income Tax

A. Unsupported expenses - 50% rule - ₱444,666.00

Respondent's verification disclosed that supporting documents to substantiate claimed deductions were not provided by petitioner; hence, 50% of the following expenses were disallowed as deductions from its gross income pursuant to Section 34(A)(1) of the NIRC of 1997, as amended:[48]

Expenses	per FS	Multiplied by	Amount disallowed
Operating expenses			
Taxes and licenses	₱ 94,673.00	50%	₱ 47,336.50
Interest expense	361,200.00	50%	180,600.00
Light and water	90,453.00	50%	45,226.50
Supplies	225,416.00	50%	112,708.00
Gasoline and oil	62,910.00	50%	31,455.00

[48] Exhibit "R-27-B", BIR Records, p. 854.

Representation	19,271.00	50%	9,635.50
Repairs and maintenance	35,409.00	50%	17,704.50
TOTAL	**₱889,332.00**		**₱444,666.00**

In the Details of Discrepancies attached to the FDDA, respondent stated that since there was no means by which the correctness and accuracy of petitioner's expenses can be ascertained, 50% of the claimed expenses were disallowed following the case of *Mariano Zamora vs. Collector of Internal Revenue*, pursuant to Section 2.4 of Revenue Memorandum Circular (RMC) No. 23-2000, which states "x x x If there is a showing that expenses have been incurred but the exact amount cannot be ascertained due to absence of documentary evidence, it is the duty of the BIR to make an estimate of the deduction that may be allowable in computing the taxpayer's taxable income, bearing heavily against the taxpayer whose inexactitude is of his own making x x x"

Petitioner argues that it has no unsupported expenses. Petitioner claims that based on its protest letter[49] dated April 3, 2012, petitioner submitted to respondent a summary of its corporate operating expenses for the year 2009 that provides the details of its operating expenses, together with the official receipts, vouchers and other source documents; thus, all of the expenses incurred by petitioner were fully substantiated and proved.

The Court finds against petitioner.

Section 34(A)(1)(b) of the NIRC of 1997, as amended, provides as follows:

> "SEC. 34. *Deductions from Gross Income.* – xxx
>
> (A) *Expenses.* –
>
> (1) *Ordinary and Necessary Trade, Business or Professional Expenses.* –
>
> (a) *In General.* – There shall be allowed as deduction from gross income all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on or which are directly attributable to, the development, management, operation and/or conduct of the trade, business or exercise of a profession, including:

[49] Exhibit "P-34" (Exhibit "I"); Exhibit "R-29", BIR Records, pp. 798-799.

xxx xxx xxx

(b) *Substantiation Requirements.* – No deduction from gross income shall be allowed under Subsection (A) hereof unless the taxpayer shall substantiate with sufficient evidence, such as official receipts or adequate records: (i) the amount of the expense being deducted, and (ii) the direct connection or relation of the expense being deducted to the development, management, operation and/or conduct of the trade, business or profession of the taxpayer."

While the afore-quoted provision allows the presentation of "adequate records" aside from the official receipts in substantiating the deductible expenses, the Court finds the Summary of Operating Expenses for 2009[50], submitted by petitioner, insufficient. In its Formal Offer of Evidence, petitioner indicated that together with the said summary are the supporting receipts. However, upon perusal of the records, the alleged supporting receipts cannot be found; only the summary is present and marked as evidence for petitioner. Consequently, based on this summary alone, the Court cannot verify the nature and actual payment of the expenses indicated therein. Petitioner should have submitted the documents from which the claimed expenses were based.

Thus, for failure of petitioner to sufficiently overcome the findings of respondent, the assessment on the said item shall be sustained.

B. Undeclared sales - ₱14,695,017.86

After computation of unreported sales based on the result of extrapolated data per monitoring, a discrepancy was noted by respondent. According to her, there is a presumption of existence of revenues which were not recorded, since the business (Makati branch) started its operations in July 2009 but per Integrated Tax System, it was only registered on March 24, 2010. Hence, the taxable income of ₱14,695,017.86, as computed below, was added to gross income pursuant to Section 32 of the NIRC of 1997, as amended:

Total sales per monitoring (Convergy's Makati)	₱ 1,645,842.00*
Sales net of VAT	1,469,501.79
Divide by number of days per monitoring/surveillance	18
Average daily sales per monitoring	81,638.99
Multiply by the no. of days in 2 quarters	90
Average sales	7,347,508.93

[50] Exhibit "P-36" (Exhibit "K").

Multiply by 2 quarters	2
Average unreported sales from July - December 2009	**₱14,695,017.86**

Summary of Daily Sales:	
Period covered	**Amount**
19-Jan-10	₱ 82,009.00
20-Jan-10	107,658.00
21-Jan-10	78,986.00
22-Jan-10	89,138.00
23-Jan-10	82,025.00
24-Jan-10	61,699.00
25-Jan-10	87,776.00
26-Jan-10	115,252.00
27-Jan-10	117,784.00
28-Jan-10	102,845.00
29-Jan-10	99,757.00
30-Jan-10	72,810.00
31-Jan-10	56,515.00
1-Feb-10	96,636.00
2-Feb-10	98,479.00
3-Feb-10	97,056.00
4-Feb-10	102,781.00
5-Feb-10	96,636.00
Total	**₱1,645,842.00***

Petitioner refutes said assessment for being speculative, hypothetical, and fictional; the same being based on mere "extrapolation" unsupported by written testimony or report of a duly authorized personnel, who is professionally competent to perform statistical computations, as there is lack of such competence on the part of the Revenue Officers who conducted the extrapolation process. As a consequence, petitioner's right to due process of law was clearly violated by the ruling of respondent, which is not supported by any substantial evidence, but only by whimsical and capricious presumptions.

The Court finds that assessments issued based on extrapolation method are valid pursuant to and subject to compliance with the provisions of Section 6(C) of the NIRC of 1997, as amended, and as implemented by Revenue Memorandum Order (RMO) No. 003-09 dated January 15, 2009, which respectively state that:

"SEC. 6. *Power of the Commissioner to Make Assessments and Prescribe Additional Requirements for Tax Administration and Enforcement.* –

xxx xxx xxx

(C) *Authority to Conduct Inventory-taking, Surveillance and to Prescribe Presumptive Gross Sales and Receipts.* – The Commissioner may, at any time during the taxable year, order inventory-taking of goods of any taxpayer as a basis for determining his internal revenue tax liabilities, or may place the business operations of any person, natural or juridical, under observation or surveillance if there is reason to believe that such person is not declaring his correct income, sales or receipts for internal revenue tax purposes. The findings may be used as the basis for assessing the taxes for the other months or quarters of the same or different taxable years and such assessment shall be deemed *prima facie* correct.

When it is found that a person has failed to issue receipts and invoices in violation of the requirements of Sections 113 and 237 of this Code, or when there is reason to believe that the books of accounts or other records do not correctly reflect the declarations made or to be made in a return required to be filed under the provisions of this Code, the Commissioner, after taking into account the sales, receipts, income or other taxable base of other persons engaged in similar businesses under similar situations or circumstances or after considering other relevant information, may prescribe a minimum amount of such gross receipts, sales and taxable base, and such amount so prescribed shall be *prima facie* correct for purposes of determining the internal revenue tax liabilities of such person."

"REVENUE MEMORANDUM ORDER NO. 003-09

SUBJECT: *Amendment and Consolidation of the Guidelines in the Conduct of Surveillance and Stock-Taking Activities, and the Implementation of the Administrative Sanction of Suspension and Temporary Closure of Business*

xxx xxx xxx

V. GUIDELINES AND PROCEDURES

A. *Surveillance Activities*

xxx xxx xxx

2. Conduct of Surveillance

xxx xxx xxx

2.4. Performance of Surveillance Activities

Generally, surveillance may be either covert or overt. Covert surveillance will eventually become overt surveillance once the implementing officer informs the SUBJECT of his presence and purpose.

xxx xxx xxx

3. Analysis of Surveillance Results

3.1. Extrapolate the data gathered from the surveillance by using the following formulas:

To get the Average Daily Sales:

$$\frac{\textit{Total Sales During Surveillance}}{\textit{Total No. of Days under Surveillance}} = \textit{Average Daily Sales (ADS)}$$

To get the Average Quarterly Sales:

ADS x 30 days x 3 months = Average Quarterly Sales (AQS)

3.2. Compare the extrapolated data with the recently filed monthly/quarterly internal revenue tax returns to determine significant variations in sales/revenues.

3.3. Determine violations of internal revenue laws, rules and regulations of the SUBJECT such as the usage of unregistered CRM/POS or invoices/official receipts and non-issuance of invoices/official receipts.

4. Action on Surveillance Results

If after the conclusion of the surveillance, there is a sufficient ground for the closure of the establishment as provided for under Section 115 of the NIRC, as amended, a recommendation shall be made to effect such closure.

> If the result of the surveillance made likewise indicates that the taxpayer had not been, in fact, correctly reporting income for tax purposes, and that the veracity of his accounting records is not reliable, the Commissioner or Regional Director concerned shall issue a Letter of Authority (LA) for the investigation of the taxpayer. The Revenue Officer named in the LA shall proceed with the audit and cause the assessment of the taxpayer's internal revenue tax liabilities, based either on: (1) surveillance, pursuant to Section 6 [C]; (2) best evidence rule, as provided under Section 6 [B], NIRC as amended; and/or (3) the result of the tax audit."

Based on the foregoing, respondent may use the results of the surveillance as basis for assessing the taxes for the other months or quarters of the same or different taxable years if there is reason to believe that such person is not declaring his correct income, sales or receipts for internal revenue tax purposes and such assessment shall be deemed *prima facie* correct.

In this case, relative to the Confidential Information filed against petitioner for alleged tax evasion through non-issuance of BIR-registered official receipts, respondent monitored the daily sales of petitioner under open surveillance to ascertain if there were, indeed, under-declarations of sales made by petitioner through deliberate non-issuance of BIR-registered official receipts. The daily sales gathered by respondent during the monitoring period of January 19, 2010 to February 5, 2010 were used by respondent in arriving at the unreported sales from July to December 2009.

Since there is sufficient reason to believe that petitioner had undeclared sales and considering that no evidence was presented by petitioner to controvert the findings of respondent, resorting to surveillance and to extrapolation method in assessing petitioner for undeclared sales are justified and in accordance with Section 6(C) of the NIRC of 1997, as amended. Consequently, the sales amounts used by respondent can be considered as *prima facie* valid and correct for purposes of determining the internal revenue tax liabilities of petitioner. Accordingly, the deficiency income tax on the undeclared sales of ₱14,695,017.86 shall be sustained.

C. Overclaimed expenses - ₱39,733.00

Respondent's verification disclosed that petitioner's total declared itemized deduction per Income Tax Return (ITR) amounting to ₱17,230,841.00 exceeded the total deductions presented per Audited Financial Statement (AFS) amounting to ₱17,191,108.00 by ₱39,733.00; hence, the over-claimed expense was disallowed as deduction from gross income pursuant to Section 34(A)(1) of the NIRC of 1997, as amended. Details are as follows:[51]

[51] Exhibit "R-27-B", BIR Records, p. 853.

Total itemized deduction per ITR		₱17,230,841.00
Less: Expenses per AFS		
Employees compensation and other benefits	₱ 276,875.00	
Taxes and licenses	94,673.00	
Interest expenses	361,200.00	
Light and water	90,453.00	
Supplies	225,416.00	
Salaries and 13th month	13,874,224.00	
Subcontractors	354,926.00	
Gasoline and oil	62,910.00	
Representation	19,271.00	
Repairs and maintenance	35,409.00	
Rent	1,769,936.00	
Depreciation	25,815.00	17,191,108.00
Overclaimed expenses		**₱ 39,733.00**

Since petitioner did not refute this finding of respondent, the Court finds that the assessment pertaining thereto should be sustained.

D. Unsupported creditable tax withheld - ₱1,084,798.00

Respondent disallowed the total creditable withholding taxes claimed by petitioner amounting to ₱1,084,798.00 for the latter's failure to support the same with sufficient evidence in accordance with Section 2.58.3(B) of RR No. 2-98, as amended.

Petitioner refutes such disallowance, contending that it submitted to respondent the Certificates of Creditable Tax Withheld at Source (BIR Form No. 2307) in support of its claimed creditable withholding taxes.

A perusal of the BIR records reveals that petitioner submitted various creditable withholding tax certificates. However, the same were mere photocopies which are either not signed or issued not under the name of petitioner. Moreover, there was no Summary Alphalist of Withholding Tax Agents (SAWT), accounting records, invoices or receipts submitted in order to verify the validity of such sales. Therefore, the creditable taxes claimed per ITR are still considered unsupported.

Considering that petitioner failed to submit before this Court the contested Certificates of Creditable Tax Withheld at Source (BIR Form No.

2307) in support of its claimed creditable withholding taxes, respondent's disallowance of the same shall be sustained.

In sum, respondent's deficiency income tax assessment is upheld. As a result, petitioner shall be held liable for basic deficiency income tax of ₱5,638,563.46, as shown below:

Taxable income/ (loss) per ITR		₱ 3,750,458.00
Add: Adjustments / disallowance		
Unsupported Expenses - 50% rule	₱ 444,666.00	
Undeclared Sales	14,695,017.86	
Overclaimed Expense	39,733.00	15,179,416.86
Taxable Income per Audit		18,929,874.86
Basic Income Tax Due (30%)		5,678,962.46
Less: Tax paid per ITR		
Payment	40,399.00	
Creditable tax withheld	1,084,798.00	
Total	1,125,197.00	
Less: Unsupported Creditable tax withheld	₱ 1,084,798.00	40,399.00
Basic Deficiency Income Tax		**₱5,638,563.46**

II. Deficiency Value-added Tax

A. Sales not subject to VAT - ₱89,433,742.28

Comparison of sales per VAT returns as against sales per ITR of petitioner disclosed that there are items which were not subjected to VAT. The amount of ₱89,433,742.28 was assessed by respondent pursuant to Section 106 of the NIRC of 1997, as amended, as implemented by Revenue Regulations No. 16-2005, as amended. Computation per Details of Discrepancy is as follows:[52]

Total sales per audit investigation	₱ 111,659,176.86
Sales per VAT returns	22,225,434.58
Sales not subjected to VAT	**₱ 89,433,742.28**

[52] Exhibit "R-27-B", BIR Records, p. 852.

The total sales per audit investigation is composed of the sales per ITR amounting to ₱96,964,159.00[53] and undeclared sales per deficiency income tax assessment amounting to ₱14,695,017.86, totaling ₱111,659,176.86.

Petitioner asserts that its total sales per AFS amount to ₱96,964,159.00, which include sales to companies that are VAT zero-rated. As such, respondent erred when she considered that the transactions of petitioner with the zero-rated corporate entities should have been subjected to VAT.

An examination of the Summary of Official Receipts issued to Clients[54] submitted by petitioner before this Court shows that petitioner's declared sales of ₱96,964,159.00 consist of zero-rated sales of ₱74,738,721.17 and VATable sales of ₱22,225,437.83.

To prove that it rendered sales subject to zero-rating, petitioner submitted the PEZA Certification of its clients, namely; Convergys Philippines Services Corporation (CPSC)[55], Analog Devices Gen. Trias, Inc. (ADGT)[56], Toshiba Information Equipment (Philippines), Inc. (TIEPI)[57], and ON Semiconductor Philippines, Inc. (OSPI).[58]

However, those PEZA Certifications were denied admission by this Court in the Resolution[59] dated September 10, 2014. Thus, the Court cannot give credence to said exhibits. Moreover, petitioner did not offer in evidence its zero-rated official receipts to prove that it actually rendered services to its clients. This means that petitioner failed to discharge the burden of proving that its sales in the amount of ₱74,738,721.17 are subject to zero-rating. Consequently, the deficiency VAT on the said item of assessment shall be sustained.

Likewise, as stated earlier, petitioner had undeclared sales of ₱14,695,017.86. Accordingly, the deficiency VAT assessment thereon should be upheld pursuant to Section 108 of the NIRC of 1997, as amended.

B. Unsupported input taxes - ₱2,606,964.98

Respondent disallowed petitioner's claimed input taxes in the amount of ₱2,606,964.98 for its failure to submit the required VAT invoices or official

[53] Exhibit "R-1", BIR Records, p. 623.
[54] Exhibit "P-37" (Exhibit "L"), docket, vol. III, pp. 1790-1794.
[55] Exhibit "P-10" (Exhibit "F-4"), docket, vol. III, p. 1732.
[56] Exhibit "P-11", docket, vol. III, p. 1733.
[57] Exhibit "P-12" (Exhibit "F-4-B"), docket, vol. III, p. 1734.
[58] Exhibit "P-13" (Exhibit "F-4-C"), docket, vol. III, p. 1735.
[59] Docket, vol. IV, pp. 1923-1924.

receipts in support thereto, pursuant to Section 110(A)(1) of the NIRC of 1997, as amended.

Petitioner contends that it has no unsupported input taxes for it was able to submit to respondent a Summary of Input Tax which was supported by sales invoices. However, respondent allegedly refused to acknowledge its receipt or to admit the foregoing evidence.

This Court cannot subscribe to petitioner's allegation that it has submitted the sales invoices in support of its claimed input taxes, which were not acknowledged by respondent. Petitioner's bare allegations are far from sufficient proof for the Court to rule in its favor. It is basic in the rule of evidence that bare allegations, unsubstantiated by evidence, are not equivalent to proof. In short, mere allegations are not evidence.[60]

Granting, without admitting that the said supporting documents were denied admission by respondent, petitioner could have easily presented and formally offered the same before this Court. However, what petitioner offered in evidence was only the Summary of Input Tax[61], without the supporting invoices; which was even denied admission by this Court per Resolution[62] dated September 10, 2014 for petitioner's failure to present the original for comparison.

As such, the Court finds no cogent reason to disturb the assessment by respondent.

However, contrary to the findings of respondent, petitioner's claimed input taxes, based on its Quarterly VAT Returns[63] for taxable year 2009, amount to ₱2,409,031.60 only. Therefore, only the said amount of ₱2,409,031.60 shall be disallowed as petitioner's input tax credit.

In sum, the Court finds petitioner liable for basic deficiency VAT in the amount of ₱13,182,288.12, computed as follows:

Vatable Sales per Return		₱ 22,225,437.47
Add: Sales Not subjected to VAT		
Alleged Zero-rated Sales	₱74,738,721.17	
Undeclared Sales	14,695,017.86	89,433,739.03
Adjusted Vatable Sales		111,659,176.50
Output Tax		13,399,101.18

[60] *Real vs. Belo*, G.R. No. 146224, January 26, 2007.
[61] Exhibit "P-39" (Exhibit "N"), docket, vol. III, pp. 1817-1887.
[62] Docket, vol. IV, p. 1923.
[63] Exhibit "R-1", BIR Records, pp. 654-657.

Less: Creditable Input Tax		
Claimed Input Taxes	₱ 2,409,031.60	
Less: Unsupported Input Taxes	2,409,031.60	-
VAT Payable		13,399,101.18
Less: Tax Paid per Return		216,813.06
Basic Deficiency VAT		**₱13,182,288.12**

III. Deficiency Tax on Improperly Accumulated Earnings

Respondent's verification disclosed that petitioner failed to withhold and remit the corresponding IAET due amounting to ₱329,022.90, pursuant to Section 29 of the NIRC of 1997, as amended, in relation to Revenue Memorandum Circular (RMC) No. 35-2011, computed as follows:[64]

Taxable income per ITR		₱3,750,458.00
Add: Overclaimed expense		39,733.00
Taxable income per audit		3,790,191.00
Less: Income tax paid for the year		1,125,137.00
Total		2,665,054.00
Add: Retained earnings from prior years	₱3,625,175.00	
Less: Paid up capital	3,000,000.00	625,175.00
IAET Income		3,290,229.00
Multiply by tax rate		10%
Basic tax due		**₱329,022.90**

Section 29(C) of the NIRC of 1997, as amended, provides:

"SEC. 29. *Imposition of Improperly Accumulated Earnings Tax.* –

(A) *In General.* – In addition to other taxes imposed by this Title, there is hereby imposed for each taxable year on the improperly accumulated taxable income of each corporation described in Subsection B hereof, an improperly accumulated earnings tax equal to ten percent (10%) of the improperly accumulated taxable income.

(B) *Tax on Corporations Subject to Improperly Accumulated Earnings Tax.* –

(1) *In General.* – The improperly accumulated earnings tax imposed in the preceding Section shall apply to every corporation formed or availed for the purpose of

[64] Exhibit "R-27-B", BIR Records, p. 852.

avoiding the income tax with respect to its shareholders or the shareholders of any other corporation, by permitting earnings and profits to accumulate instead of being divided or distributed.

(2) *Exceptions.* – The improperly accumulated earnings tax as provided for under this Section shall not apply to:

(a) Publicly-held corporations;
(b) Banks and other nonbank financial intermediaries; and
(c) Insurance companies.

(C) *Evidence of Purpose to Avoid Income Tax.* –

(1) *Prima Facie Evidence.* – The fact that any corporation is a mere holding company or investment company shall be *prima facie* evidence of a purpose to avoid the tax upon its shareholders or members.

(2) *Evidence Determinative of Purpose.* – **The fact that the earnings or profits of a corporation are permitted to accumulate beyond the reasonable needs of the business shall be determinative of the purpose to avoid the tax upon its shareholders or members** unless the corporation, by the clear preponderance of evidence, shall prove to the contrary.

(D) *Improperly Accumulated Taxable Income.* – For purposes of this Section, the term 'improperly accumulated taxable income' means taxable income' adjusted by:

(1) Income exempt from tax;
(2) Income excluded from gross income;
(3) Income subject to final tax; and
(4) The amount of net operating loss carry-over deducted;

And reduced by the sum of:
(1) Dividends actually or constructively paid; and
(2) Income tax paid for the taxable year.

> *Provided, however*, That for corporations using the calendar year basis, the accumulated earnings tax shall not apply on improperly accumulated income as of December 31, 1997. In the case of corporations adopting the fiscal year accounting period, the improperly accumulated income not subject to this tax, shall be reckoned, as of the end of the month comprising the twelve (12)-month period of fiscal year 1997-1998.
>
> (E) *Reasonable Needs of the Business.* – For purposes of this Section, the term 'reasonable needs of the business' includes the reasonably anticipated needs of the business." *(Emphasis supplied)*

The foregoing provision is implemented by RR No. 02-01, Sections 5 and 7, which provide:

> "SECTION 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).
>
> xxx xxx xxx
>
> SECTION 7. *Determination of Purpose to Avoid Income Tax.* – The fact that a corporation is a mere holding company or

investment company shall be *prima facie* evidence of a purpose to avoid the tax upon its shareholders or members. Likewise, **the fact that the earnings or profits of a corporation are permitted to accumulate beyond the reasonable needs of the business shall be determinative of the purpose to avoid the tax upon its shareholders or members**. In both instances, the corporation may, by clear preponderance of evidence in its favor, prove the contrary.

xxx xxx xxx

The following are *prima facie* instances of accumulation of profits beyond the reasonable needs of a business and indicative of purpose to avoid income tax upon shareholders:

(a) Investment of substantial earnings and profits of the corporation in unrelated business or in stock or securities of unrelated business;
(b) Investment in bonds and other long-term securities;
(c) Accumulation of earnings in excess of 100% of paid-up capital, not otherwise intended for the reasonable needs of the business as defined in these Regulations.

In order to determine whether profits are accumulated for the reasonable needs of the business as to avoid the imposition of the improperly accumulated earnings tax, the controlling intention of the taxpayer is that which is manifested at the time of accumulation, not subsequently declared intentions which are merely the product of afterthought. A speculative and indefinite purpose will not suffice. The mere recognition of a future problem or the discussion of possible and alternative solutions is not sufficient. **Definiteness of plan/s coupled with action/s taken towards its consummation are essential.**" *(Emphasis supplied)*

Meanwhile, petitioner refutes such assessment to be erroneous, claiming that it had appropriated the amount of ₱4,200,000.00, which approximately covers its retained earnings from prior years, for expansion purposes of the company.

Petitioner anchors its contentions from the same regulation which provides that the undistributed earnings and profits for the reasonable needs of the business would not generally make the accumulated or undistributed earnings subject to tax. Hence, the amount earmarked for the company's expansion is a reasonable need of its business and should not be subjected to tax.

Pertinent provisions of RR No. 2-2001, provide:

> "SECTION 3. *Determination of Reasonable Needs of the Business.* – An 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.
>
> For purposes of these Regulations, the following constitute accumulation of earnings for the reasonable needs of the business:
>
> xxx xxx xxx
>
> **(b) Earnings reserved for definite corporate expansion projects or programs requiring considerable capital expenditure as approved by the Board of Directors or equivalent body;**" *(Emphasis supplied)*

Petitioner claims that based on its Board Resolution dated December 5, 2008, the amount of "4.2 Million will be allocated/reserved for Expansion expenses on planned transfer to FTI."

However, the Court finds the foregoing allegation wanting as the details of said planned expansion or transfer was not included in the said Board Resolution, even as to where the amount of ₱4.2 Million will be sourced was not indicated and explained therein. It must be emphasized that Section 7 of RR No. 02-01 explicitly provides that a speculative and indefinite purpose will not suffice. Definiteness of plans coupled with actions taken towards its consummation are essential.

Considering that no other evidentiary documents were presented by petitioner, and that its Board Resolution was denied admission by this Court per Resolution[65] dated September 10, 2014 for petitioner's failure to identify said exhibit and for not being found in the records, petitioner's contention has no leg to stand on. As a result, the findings of respondent shall be sustained and petitioner shall be held liable for basic IAET of ₱329,022.90.

Respondent imposed a fifty percent (50%) surcharge on all the deficiency tax assessments, pursuant to Section 248 of the NIRC of 1997, as amended, for failure to file a return and/or false or fraudulent return, in relation to RMO No. 15-95, Annex A(E)(27), as amended by RMO No. 31-95, which provides that "failure to keep records, especially if put on notices by the BIR as a result of prior examination, concealment of records or refusal to make certain records available" is an indication of fraud. According to respondent, petitioner failed to present or submit its books of accounts and other accounting records for taxable year 2009 to the BIR during the administrative investigation of its case which resulted in the issuance of the BIR Subpoena Duces Tecum[66] dated September 3, 2010 and the subsequent filing by the BIR of a criminal complaint[67] against the responsible officers of petitioner for violation of Sections 5(C), 256, and 266 of the NIRC of 1997, as amended.

Well-settled is the rule in taxation that tax assessments by tax examiners are presumed correct and made in good faith. All presumptions are in favor of the correctness of a tax assessment.[68] The burden of proof is on the taxpayer to present evidence to show the incorrectness of the assessment. And considering that petitioner did not present any argument and/or evidence against respondent's imposition of the 50% surcharge, such imposition will be allowed.

In recapitulation, the Court finds that the assessments issued by respondent against petitioner for taxable year 2009 covering deficiency income tax, VAT, and IAET should be upheld.

WHEREFORE, premises considered, the instant Petition for Review is hereby **DENIED**. Accordingly, petitioner is **ORDERED TO PAY** respondent the modified amount of ₱28,724,811.72, representing basic deficiency income tax, VAT, and IAET, inclusive of the fifty percent (50%) surcharge imposed under Section 248 of the NIRC of 1997, as amended, computed as follows:

---

[65] Docket, vol. IV, p. 1923.
[66] Exhibit "R-11", BIR Records, p. 260.
[67] Exhibits "R-12" and "R-12-B", BIR Records, pp. 263-266.
[68] *Commissioner of Internal Revenue vs. Hantex Trading Co., Inc.*, G.R. No. 136975, March 31, 2005.

Tax Type	Basic	Surcharge	Total
Income Tax	₱ 5,638,563.46	₱ 2,819,281.73	₱ 8,457,845.19
Value-added Tax	13,182,288.12	6,591,144.06	19,773,432.18
Improperly Accumulated Earnings Tax	329,022.90	164,511.45	493,534.35
Total	**₱ 19,149,874.48**	**₱ 9,574,937.24**	**₱ 28,724,811.72**

In addition, petitioner is **ORDERED TO PAY**:

(a) Deficiency interest at the rate of twenty percent (20%) per annum on the basic deficiency income tax, VAT, and IAET computed from the dates indicated below until full payment thereof pursuant to Section 249(B) of the NIRC of 1997, as amended:

	Basic Deficiency Tax	Deficiency Interest computed from
Income Tax	₱ 5,638,563.46	April 15, 2010
Value-added Tax	₱ 13,182,288.12	January 25, 2010
Improperly Accumulated Earnings Tax	₱ 329,022.90	January 15, 2011

(b) Delinquency interest at the rate of 20% per annum on the total amount of ₱28,724,811.72 and on the 20% deficiency interest which have accrued as afore-stated in (a), computed from October 24, 2012 until full payment thereof pursuant to Section 249(C) of the NIRC of 1997, as amended.

SO ORDERED.

Ma. Belen
MA. BELEN M. RINGPIS-LIBAN
Associate Justice

WE CONCUR:

LOVELL R. BAUTISTA
Associate Justice

ESPERANZA R. FABON-VICTORINO
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.

LOVELL R. BAUTISTA
Associate Justice
Chairperson

CERTIFICATION

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

ROMAN G. DEL ROSARIO
Presiding Justice