Library

REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

MERCY'S INC.,
Petitioner,

- versus - C.T.A. CASE NO. 895

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

x - - - - - - - - - - - - x

MERCY ALMONIDOVAR DE VERA and JUAN A. DE VERA,
Petitioners,

- versus - C.T.A. CASE NO. 896

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

5/11/82

x - - - - - - - - - - - - x

D E C I S I O N

These are separate but jointly heard appeals from the decisions of respondent holding petitioners liable for deficiency income taxes for the years 1953 to 1956. Involving, as they do, identical tax years and allied issues, this court promulgates in these two (2) cases this joint decision.

It appears that petitioner, Mercy's Inc., in C.T.A. Case No. 895, is a corporation registered with the Securities & Exchange Commission, with principal office at 1735 Azcarraga, Manila, while petitioners, Mercy Almonidovar de Vera and Juan A. de Vera, are husband and wife residing in the same address.

After investigation of their tax liabilities by examiners from the Bureau of Internal Revenue, the respondent Commissioner of Internal Revenue assessed deficiency income tax against Mercy's Inc., for the years 1953 to 1956 in the total amount of ₱20,674.00, including 50% surcharge and compromise penalty, as follows:

1953

Net income per investigation . .	₱12,926.10
Tax due thereon	₱ 2,585.00
Add: 50% surcharge	1,293.00
Compromise for non-filing of return	50.00
TOTAL AMOUNT DUE & COLLECTIBLE .	₱ 3,928.00

1954

Net income per investigation . .	₱12,726.10
Tax due thereon	₱ 2,545.00
Add: 50% surcharge	1,273.00
Compromise for non-filing of return	50.00
TOTAL AMOUNT DUE & COLLECTIBLE .	₱ 3,868.00

1955

Net income per investigation . .	₱16,466.10
Tax due thereon	₱ 3,293.00
Add: 50% surcharge	1,647.00
Compromise for non-filing of return	50.00
TOTAL AMOUNT DUE & COLLECTIBLE .	₱ 4,990.00

1956

Net income per investigation . .	₱26,126.10
Tax due thereon	₱ 5,225.00
Add: 50% surcharge	2,613.00
Compromise for non-filing of return	50.00
TOTAL AMOUNT DUE & COLLECTIBLE .	₱ 7,888.00

(Exh. 9, pp. 25-36, BIR rec., CTA No. 895)

and against Mercy Almonidovar de Vera for the same years in the aggregate amount of ₱51,923.00 (Exh. 22, Vol. I, BIR rec., pp. 145-147, CTA No. 896) including 50% surcharge and compromise penalty, as follows:

1953

Undeclared rental income from Mercy Bldg.	₱ 8,100.00
Rental income from advertisement	6,000.00
Gross undeclared income	₱14,100.00
Deduct: Rent to Bureau of Lands	8,620.00
Net income per investigation . .	₱ 5,480.00
Less: Personal exemption	3,000.00
Amount of income subject to tax	₱ 2,480.00
Tax due thereon	₱ 89.00

Add: 50% surcharge		₱ 44.50
Compromise for non-filing of return		50.00
DEFICIENCY TAX DUE		₱ 183.50

1954

Undeclared rental income from Mercy Bldg.		₱57,150.00
Rental income from advertisement		6,000.00
Gross undeclared income		₱63,150.00
Deduct:		
Depreciation of Mercy Bldg. . .	₱4,444.44	
Lease rental expense to Bureau of Lands	8,620.00	13,064.44
Net income per investigation . .		₱50,085.56
Less: Personal exemption . . .		3,000.00
Amount of income subject to tax.		₱47,085.56
Tax due thereon		₱13,054.00
Add: 50% surcharge		6,527.00
Compromise for non-filing of return		300.00
DEFICIENCY TAX DUE		₱19,881.00

90-EAR-24468-59/55

Net loss disclosed by the return as audited		(₱ 8,532.67)
Unallowable deductions & additional income:		
Undeclared rental income from Mercy Bldg.	₱76,265.00	
Advertisement rental income	6,000.00	
Gross undeclared income	₱82,265.00	
Deduct:		
Depreciation on Mercy Bldg.	₱8,888.88	

Lease rental expense to Bureau of Lands . .	8,620.00	17,508.88	64,756.12
Net income per investigation			₱56,223.45
Less: Personal exemption			3,000.00
Amount of income subject to tax . .			₱53,223.45
Tax due thereon			₱15,574.00
Add: 50% surcharge			₱ 7,787.00
Compromise for filing fraudulent return			300.00
DEFICIENCY TAX DUE			₱23,661.00

90-EAR-112045-59/56

Net income disclosed by the return as audited		₱ 5,261.68
Unallowable deductions & additional income:		
Undeclared rental income from Mercy Bldg.	₱ 7,463.00	
Advertisement rental income	6,650.00	
Overclaimed depreciation on Mercy Bldg.	11,111.12	
Lease rental expense to Bureau of Lands disallowed	4,380.00	29,604.12
Net income per investigation		₱34,865.80
Less: Personal exemption		3,000.00
Amount of income subject to tax . .		₱31,865.80
Tax due thereon		₱ 5,265.00
Add: 50% surcharge		2,632.50
Compromise for filing fraudulent return		300.00
DEFICIENCY TAX DUE		₱ 8,197.50

The deficiency income tax assessment against Mercy's Inc. is premised on its failure to file returns for the years in question. With respect to Mercy Almonidovar de Vera, the assessment is anchored on her failure to file income returns for 1953 and 1954 and the filing of false and fraudulent returns for 1955 and 1956.

Mercy Almonidovar de Vera as general manager of Mercy's Inc. and in her own behalf, in separate letters on different dates, disputed the aforesaid assessments and requested reconsideration on the grounds that the investigation was conducted without due process and there were mistakes in the computation of respondent. (Exh. 11, p. 39, BIR rec., CTA No. 895; Exh. 23, pp. 149-150, Vol. I, BIR rec., CTA No. 396). Both request were, however, denied and respondent reiterated the demand for payment of the deficiency income tax assessed. (Exh. 12, p. 58, BIR rec., CTA No. 895; Exh. 24, p. 158, BIR rec., Vol. I, CTA No. 896).

Not satisfied with the decisions of respondent, petitioners appealed to this Court.

In answers to the petitions for review, respondent prayed for affirmance of the assessments involved.

These cases present a common issue, i.e. whether or not the deficiency income tax assessments issued against petitioners are legal, and the additional question raised in CTA Case No. 896, which is whether or not the assessment for 1953 has already prescribed.

At the outset, it can be stated that the records of these cases clearly show that respondent's assessments are primarily based on the examiners reports which are not well founded. Respondent's examiners who investigated petitioners tax liabilities did not conduct a thorough investigation. They did not secure or show any evidence to prove that Mercy Building is owned by Mercy's Inc. They did not verify where the income of said building really go during the years covered by the assessment. They cannot really say that petitioners intended to evade payment of the tax; and the fact that two assessments were issued, one against Mercy Bldg., and the other against Mercy Almonidovar de Vera, computed on the basis of tax on individual, which remained unexplained.

Respondent makes much of the circumstance that Mercy Almonidovar de Vera and Mercy's Inc. refused examination of her books and that of Mercy's Inc., despite repeated demands and duly issued subpoena duces tecum. These circumstances cannot justify an inference that the taxpayer committed certain violations under the Revenue Code.

In connection with CTA Case No. 895, it must be noted that respondent's assessment is based on the report of the examiners alleging failure of Mercy's Inc. to file returns from 1953 to 1956 inspite of the receipt of income from Mercy Building it supposedly own. In other words, the assessment rests on the alleged ownership of Mercy Building by Mercy's Inc. This basis, however, is belied by the very same report which states that Mercy Almonidovar de Vera is the registered owner of said building. Needless to say, the income therefrom cannot be considered as income of Mercy's Inc. Respondent could have check from the return of Mercy Almonidovar whether the income from said building was included in her return. And, respondent could have explained why the assessment against Mercy's Inc. was computed on the basis of the tax on individuals.

We are convinced by the explanation offered by petitioners during trial that the taxpayer's mistake in not consolidating all her income is committed in good faith and evidence showed that she did include the income from Mercy Building in her return. Moreover, in the absence of any indication that Mercy Inc. received income during the years in question, its failure to file income tax return for those years, were of no consequence.

Considering therefore, the surrounding circumstances, the assessment against Mercy's Inc. is not proper.

We now come to CTA Case No. 896. In this case, the returns of petitioners for 1953, 1954, 1955 and 1956 were due for filing on March 1, 1954, 1955, 1956 and 1957, respectively. It is now urged that respondent's right to assess the deficiency income tax for 1953 has already prescribed. Petitioners argue that since the return for 1953 was filed on March 1, 1954 and notice of the assessment was only received on September 22, 1959, the five year period for assessment provided in Section 331 of the Revenue Code has already elapsed. Respondent on the other hand, maintains that the ten year period provided in Section 332, for assessment should apply because petitioners failed to file the returns for 1953 and 1954.

Respondent, obviously overlooked Section 45 of the same Code, then applicable to the case at bar, the pertinent provision of which states:

> "Sec. 45. Individual returns. x x x.
>
> (b) Where to file.- The return shall be filed with the Commissioner of Internal Revenue, provincial revenue agent, or treasurer of the province, city, or municipality in which such person has his legal residence or principal place of business in the Philippines, then with the Commissioner of Internal Revenue in Manila."
>
> x x x x x x x x x.

Evidence reveals that the taxpayer has complied with the requirements of the law by filing the return for 1953 with the Office of the City Treasurer of Manila as shown by the duplicate copy, stamped by said office March 1, 1954. (Exh. A, pp. 63-64, CTA rec., CTA No. 895). Evidence also shows that a copy of the income tax return of Mercy Almonidovar de Vera which reflect rental income of ₱60,200.00 (Vet. Hunter's Bldg.) for 1954 was received by the Income Tax Division of the Bureau of Internal Revenue on March 1, 1955. (Exh. B, pp. 65-68, CTA rec., CTA No. 895). We also noted that respondent merely stood pat on his argument that petitioners failed to file returns for 1953 and 1954. In short, petitioners' returns were disregarded.

In this light, we are of the persuasion that respondent's right to assess the deficiency income tax for 1953 has already prescribed. So, we now come to the question of the legality of the assessment against petitioners for 1954 to 1956.

For these years, respondent asserts that there are sufficient evidence to establish a <u>prima facie</u> case of tax evasion against Mercy

Almonidovar de Vera. Said assessment could have been sustained had respondent made proper verification from all sources and established that petitioners really evaded the payment of tax, but, as indicated earlier, respondent's assessments are not well founded.

While we are of the opinion that the evidence on record does not justify the assessment in question, we believe that some of petitioners returns need revision.

With respect to 1953, nothing justify revision of the return because respondent's right to assess has already prescribed.

With respect to 1954, respondent asserts that petitioners have undeclared rental income of ₱57,150.00 from Mercy Building and ₱6,000.00 rental income from advertisement. The return filed however, reflected the amount of ₱60,200.00 as rental income (Exh. B, <u>supra.</u>) and petitioners' witness, testifying in open court, explained that the advertisement income of ₱6,000.00 was included in the rental income reported. (See pp. 14-16, t.s.n., Hearing of June 3, 1963). To our mind, therefore, there is no undeclared rental income for 1954.

Be that as it may, petitioners deducted among others, rental expense in the amount of ₱15,460.00 and depreciation on (Vet. Hunter's Bldg.) Mercy Inc. Building in the amount of ₱10,500.00.

On the rental expenses, what may only be considered deductible is ₱8,620.00 which is duly supported by the lease contract between Mercy Almonidovar de Vera and the Bureau of Lands. (Exh. 25, pp. 21-23, Vol. II, BIR rec., CTA No. 896). As regards the depreciation, contrary to petitioners pretension, it appears that respondent applied consistent rates. (See Exh. 21, pp. 9-16, Vol. II, BIR rec., CTA No. 896). Hence, petitioners return for 1954 should be revised accordingly and to take into consideration the other items of deduction which respondent did not controvert.

With respect to 1955, one thing that strikes us is that petitioners return showed a gross rental income of ₱99,072.00, as against respondent's finding of only ₱82,265.00 (See Exh. E, p. 79, CTA rec., CTA No. 895 and Exh. 22, _supra_.) Even the amount of ₱97,105.00 as rental income indicated in the examiners' worksheet, (Exh. 21, _supra_.) is less than that declared in petitioners return.

This notwithstanding, we believe that petitioners return for 1955 needs revision to the effect that as in 1954, they should not only be allowed depreciation of ₱4,473.90 on Mercy Inc. Bldg.; ₱8,888.88 on Mercy Bldg.; and rental expense of ₱8,620.00; and also the other items not disputed by respondent.

With respect to 1956, it appears that petitioner Mercy Almonidovar de Vera filed her return on March 27, 1957 (pp. 67-68, Vol. I, BIR rec., CTA No. 896). This was subsequently amended on October 29, 1957. (Exh. D, pp. 68, CTA rec., CTA No. 896). The original as well as the amended return reported a gross rental income of ₱101,642.00. Respondent, however, insists that petitioners realized a gross rental income of ₱109,105.00.

After evaluating the evidence on record in relation to the 1956 return, we are convinced that the undeclared rental income averred by respondent has already been included in the return and the overclaimed depreciation and rental expense would not in any way alter the result because many items deducted by petitioners were never disputed by respondent. Hence, there is no necessity of revising petitioners returns.

In fine, the deficiency income tax liability of petitioners for 1954 and 1955 is computed as follows:

1954

Gross income per return		₱ 68,660.50
Deduct: Rent to the Bureau of Lands	₱ 8,620.00	
Depreciation on Mercy Inc. Bldg.	4,473.90	
Depreciation on Mercy Bldg. ..	4,444.44	
Other deductions not disputed..	41,080.00	58,618.34
Net income		₱ 10,042.16
Less personal exemption		3,000.00
Amount subject to tax		₱ 7,042.16
DEFICIENCY TAX DUE		₱ 667.00

1955

Gross income per return		₱99,072.00
Deduct: Rent to the Bureau of Lands	₱ 8,620.00	
Depreciation on Mercy Inc. Bldg.	4,473.90	
depreciation on Mercy Bldg. ..	8,888.88	
Other deductions not disputed..	40,282.88	62,265.66
Net income		₱36,806.34
Less personal exemption		3,000.00
Amount subject to tax		₱33,806.34
DEFICIENCY TAX DUE		₱ 7,990.00

As regards the 50% fraud penalty for all the years in question, it is the well established rule that fraud is not to be presumed, and it is incumbent upon respondent to prove its existence to justify its imposition. (William Li Yao v. Coll., CTA Case No. 30, July 31, 1956; Marguerite Wolfson v. Coll., CTA Case No. 273, July 16, 1958; Antigua v. Coll., CTA Case No. 579, Nov. 2, 1959; Tumambing v. Coll., CTA Case No. 69, July 12, 1961). Moreover, fraud is a serious charge and to be sustained, it must be supported by clear and convincing proof. (Araneta v. Comm., CTA Case No. 1699, Nov. 6, 1970).

Anent the compromise penalty, suffice it to state that respondent is not authorized to impose the same without the taxpayers consent. (Coll. v. U.S.T. et al., 104 Phil. 1962; Coll. v. Bautista, 105 Phil. 1326; Phil. Int'l. Fair v. Coll., 4 SCRA 774).

WHEREFORE, the appealed decision in CTA Case No. 895 is hereby declared illegal and improper and, therefore, set aside.

The appealed decision in CTA Case No. 896 is hereby modified and petitioners Mercy Almonidovar de Vera and Juan A. de Vera are ordered to pay respondent Commissioner of Internal Revenue the aggregate amount of ₱8,657.00 representing deficiency income tax for the years 1954 and 1955 as computed above plus 5% surcharge and 1% monthly interest that have accrued thereon from November 1, 1959, provided the maximum amount that may be collected as interest on the deficiency shall in no case exceed the amount corresponding to a period of three (3) years pursuant to Section 51 (e) of the Tax Code, as amended by Republic Act No. 2343.

Without pronouncement as to costs.

SO ORDERED.

Quezon City, May 11, 1982.

CONSTANTE C. ROAQUIN
Associate Judge

I CONCUR:

AMANTE FILLER
Presiding Judge

Took no part

ALEX Z. REYES
Associate Judge