REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

FIRST DIVISION

FAX N PARCEL, INC., Petitioner,	CTA CASE NO. 7415
	Members:
- versus -	ACOSTA, *Chairperson* UY, *and* FABON-VICTORINO, *JJ.*
COMMISSIONER OF INTERNAL REVENUE, Respondent.	Promulgated: NOV 22 2011 ; 10:07 am

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DECISION

FABON-VICTORINO, J.:

Before the Court is a Petition for Review filed by petitioner Fax N Parcel Inc. praying for the cancellation of the assessments allegedly issued by respondent Commissioner of Internal Revenue (CIR) for deficiency income tax (IT) and value-added tax (VAT) for the fourth (4th) quarter of 2002.

Petitioner avers that it is a duly organized local corporation engaged in the business of transmitting information through different mediums of communication, such as but not limited to telephones, telegraphs, facsimile and other over-the-counter-related services. Its principal place of business is at Unit 33 LGF Building A, SM Megamall, EDSA, Mandaluyong City.[1]

Respondent, on the other hand, is the Commissioner of the Bureau of Internal Revenue (BIR) empowered to issue and cancel disputed assessments. She holds office at the BIR National Office Building, BIR Road, Agham, Quezon City.

On March 18, 2005, respondent issued against petitioner a Preliminary Assessment Notice (PAN),[2] with attached Details of Discrepancies[3] for unreported income from understatement of sales in the amount of P3,195,663.73 on purchases made by third parties during the 4th quarter of 2002. Petitioner received the PAN and the Details of Discrepancies on March 18, 2005.[4]

On April 28, 2005, respondent issued a Formal Assessment Notice (FAN)[5] with another Details of Discrepancies,[6] which was

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[1] Par. 1, Petition for Review.
[2] Exhibit "3".
[3] Exhibit "D" and "3-C".
[4] Exhibit "3".
[5] Exhibit "4".
[6] Exhibit "4-b".

but a reiteration of the Details of Discrepancies[7] issued on March 18, 2005. They were received by petitioner on April 30, 2005.[8]

On May 30, 2005, petitioner filed a Protest Letter,[9] and submitted supporting documents on July 29, 2005.[10] Respondent however failed to act on the said protest within the required 180-day period from petitioner's submission of supporting documents.[11] Hence, this Petition for Review filed on February 24, 2006.

In her Answer dated May 19, 2006, petitioner raised the following Special and Affirmative Defenses:

> ***"A) Deficiency Income Tax:***
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> 11) Pursuant to Revenue Regulations (RR) No. 7-95 dated 4 December 1995, as amended by RR 13-97 and 7-99 dated 18 November 1997 and 10 February 1999, respectively, which was duly approved by the Secretary of Finance upon the recommendation of the Commissioner of Internal Revenue, the Bureau of Internal Revenue made mandatory the submission of the Summary List of Sales and Purchases (SLSP) of all persons liable for VAT;

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[7] Exhibit "D" and "3-C".
[8] Exhibit "4".
[9] Summary of Admitted Facts, par. 2, Respondent's Pre-Trial Brief dated July 04, 2006, docket p. 71; Exhibit "B" and "7".
[10] Par. 1, Stipulation of Facts, Joint Stipulation of Facts, docket p. 78; Exhibit "C".
[11] Par. 2, Stipulation of Facts, Joint Stipulation of Facts, docket p. 78.

12) Verification disclosed that based on the Summary List of Purchases submitted by Petitioner's customers for the 4th quarter of 2002, Petitioner made a gross sale of P5,007,571.73, however, Petitioner's VAT return for the 4th quarter reflected a gross sales of only P1,811,908.00, hence, Petitioner has an undeclared income from its undeclared sales in the amount of P3,195,663.73, which is subject to income tax in the amount of P1,968,738.98, inclusive of surcharge and interest;

B) Deficiency Value Added Tax:

13) The 1997 Tax Code provides that 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 10% value added tax on the gross selling price or gross value in money in cases of sale, barter or exchange of goods or properties; or on the gross receipt in cases of sale or exchange of services, including the use or lease of properties (*Sections 105, 106 & 108*);

14) As mentioned in the preceding paragraphs, Petitioner made an under declaration of its sale in the amount of P3,195,663.73, such sale is subject to VAT at 10% or an amount of P629,239.32, inclusive of surcharge and interest;

C) Deficiency Assessments:

15) Contrary to the claim of Petitioner, the exact amounts of its deficiency income and value added taxes were stated in the Formal Assessment Notice (FAN), which was attached to the Details of Discrepancies, further, Petitioner

received the FAN on 30 April 2005, hence, this date should be the reckoning point for the prescriptive period for the filing of the protest and other subsequent actions;

16) 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. All presumptions are in favor of tax assessments (*Interprovincial Autobus Co., Inc. v. Collector, 98 Phil. 290*; *Cecilia Teodoro Dayrit v. Hon. Fernando Cruz and Commissioner, L-39910, Sept. 26, 1988*; *Bonifacia Sy Po v. CTA & Commissioner, G.R. No. 81446, Aug. 18, 1988, all cases cited in Aban, Law of Basic Taxation in the Philippines, 1st Edition, p. 109*);"

To expedite the proceeding, the parties submitted a Joint Stipulation of Facts on July 27, 2006,[12] which the Court approved on September 7, 2006, thereby terminating the pre-trial conference.

Trial ensued with petitioner presenting its first witness MA. ELENA T. ESPIRITU, its accounting manager.

She testified that after filing its VAT Return for 2002, petitioner received from the BIR Details of Discrepancies dated

[12] Docket, pp. 78-80.

March 18, 2005[13] with attached Quarterly Report on Third Party Information on Purchases.[14]

This was followed by another Details of Discrepancies dated April 28, 2005[15] received by petitioner on May 24, 2005, assessing it for alleged VAT deficiency for its sales during the fourth quarter of 2002 and for deficiency IT. The assessment was allegedly based on third party information received by the BIR from the customers of petitioner.

Petitioner filed a protest[16] to the assessment stating that the amounts allegedly reported by the third party customers were different from those reflected in petitioner's record of actual purchases of the named customers. The amounts cited ranging from hundreds of thousands to millions of pesos were unrealistic since petitioner was just a small enterprise engaged in photocopying, fax and courier services.

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[13] Exhibit "D".
[14] Exhibit "E".
[15] Exhibit "A".
[16] Exhibit "B" and "7".

The witness further testified that petitioner's transactions range from as low as P2.00 to a couple of hundreds, except for their courier service transactions which range from P1,500.00 to P3,000.00. During the fourth quarter of 2002, petitioner had only two photocopying machines, two fax machines, a computer and a printer. Even assuming full capacity operation with no downtime or lean periods, their photocopying including their fax and courier services could only generate P30,000.00, more or less. The amount allegedly reported by informant SM Mart was already equivalent to petitioner's sales for one whole month assuming that its operations would run for straight eleven hours daily.

In support of its protest, petitioner submitted to respondent the summary of its sales for October, November and December 2002,[17] together with the corresponding VAT remitted to the BIR for the same period and Form 2550Q for the fourth quarter of 2002.

On September 16, 2005, petitioner received a letter from the BIR dated September 13, 2005, indicating that its protest

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[17] Exhibits "G," "H," and "I".

had been forwarded to Revenue District Office No. 50 for appropriate action. The letter as well mentioned that the assessed amounts of P1,968,738.98 was for deficiency IT, and the P629,239.32 was for deficiency VAT, both for the fourth quarter of 2002. The said amounts however were never mentioned in the previously issued Details of Discrepancies dated April 28, 2005.

For failure of respondent to act on petitioner's protest within the allotted period of 180 days, petitioner filed the instant Petition for Review before the Court on February 24, 2006.

On September 7, 2006,[18] Ma. Elena T. Espiritu was recalled to the witness stand. She testified that the sales of petitioner were net of VAT based on its books of accounts which she personally prepared. She presented petitioner's Ledger for the months of October to December 2002.[19]

On February 8, 2007, the same witness further testified that petitioner had P6.8 Million Sales for the entire year of 2002

[18] Exhibit "A".
[19] Exhibits "N," "O," and "P".

in stark contrast with P5M sales for one quarter alleged by the BIR examiner. This was unrealistic since petitioner's Financial Statement[20] and Income Tax Return[21] for the year 2002 showed that petitioner paid an IT of only P46,233.43. Further, petitioner's Quarterly VAT Return for the fourth quarter of 2002,[22] and the Official Receipt[23] of the remittance of the VAT amounted only to P7,655.00.

To bolster its claim, petitioner moved for issuance of Subpoenas *Duces Tecum Ad Testificandum* to the third-party purchasers who allegedly submitted a summary list of their purchases from petitioner directing them to testify and bring to the Court official receipts and/or other documents pertaining to their claimed purchases from petitioner for the fourth quarter of 2002.[24]

In compliance with the subpoenas issued by the Court, Cheryl M. Joseph, Arlene Estipona, Nimfa A. Masculino, Ma. Irma Topacio, Anna May Ceredon, Marivic Trosado, Loida P. Leyson, Minerva Baguing, Jean Tiempo, Lovely Magnaye appeared and

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[20] Exhibit "M".
[21] Exhibit "R".
[22] Exhibit "K".
[23] Exhibit "L".
[24] Exhibit "Y".

identified their respective judicial affidavits and certifications executed in compliance with the Court's directive.

CHERYL M. JOSEPH, Chief Finance Officer and previously Chief Accountant of Leisure and Allied Industries Philippines, Inc (LAIPI) in 2002, testified that in the conduct of their business in SM Megamall, they occasionally utilize the photocopying services of petitioner. For the fourth quarter of 2002, the total purchases of LAIPI from petitioner amounted to P623.75, inclusive of value added tax, based on the official receipts issued by petitioner and the cash disbursement voucher for payment and books of LAIPI. She prepared a summary of LAIPI's transactions with petitioner indicating the date, particulars, gross amount, corresponding VAT, and official receipt number issued for each transaction. However, some transactions in the said summary do not have official receipt numbers as the corresponding receipts can no longer be located despite diligent search. Thus, the entries for these transactions made five (5) years ago were based on the cash disbursement voucher and/or the books of LAIPI.

On cross, she added that LAIPI is the operator of the Timezone Family Entertainment Center, a VAT registered taxpayer. She confirmed that its total purchase from petitioner for the fourth quarter of 2002 amounted to P623.75, inclusive of VAT. However only P409.55 was reflected in the Quarterly Report on Third Party Information on Purchases Per Taxpayer submitted to the BIR as their company was required to report actual purchases for the Fourth Quarter of 2002 and the purchases for the month of December were liquidated in January 2003.

On re-direct, she explained that the purchases for the month of December in the amount of P263.25 were liquidated in January 2003 for they were deemed petty cash expenses of Time Zone Megamall branch, thus were not included in the VAT liquidation for the fourth quarter of 2002.

ARLENE ESTIPONA, Accounting Officer of Arancia, Inc., testified that she has no knowledge of any transaction with petitioner either in her personal capacity or as an officer of Arancia, Inc. She has no record showing that Arancia, Inc. ever dealt with petitioner.[25]

[25] Exhibit "U".

Both ***MA. IRMA TOPACIO***, the Vice President for Finance of Music One Corporation[26] and ***MARIVIC TROSADO,*** the Finance Officer of Hi-Integra, Inc., [27] admitted that they were aware of the assessment issued by respondent against petitioner for deficiency IT and VAT for the fourth quarter of 2002. The bases of this assessment were the computer print-outs showing that Music One Corporation made purchases from petitioner in the amount of P49.00 in December 2002, while Hi-Integra, Inc., in the amount of P54.00 in October 2002. But based on their respective records, there were no such purchases made by them from petitioner during the fourth quarter of 2002.

MINERVA BAGUING, Accounting Manager of SM Mart, Inc., testified that per their record, they never purchased goods or services from petitioner during the fourth quarter of 2002 and that their company never reported to respondent any purchase from petitioner for the same period. This is contrary to the computer print-out of respondent showing that SM Mart purchased from petitioner in October, November and December

[26] Exhibit "V".
[27] Exhibit "X".

2002 in the amounts of P555,365.30, P574,387.60 and P1,306,326,70, respectively.[28]

Jean Tiempo, the Accounting Manager of Plaza Arcade, Inc., declared that petitioner had been assessed for deficiency IT and VAT for the fourth quarter of 2002. Allegedly, part of the basis of said assessment was a report of purchases of Plaza Arcade Inc., from petitioner in a computer print-out in the amounts of P87,863.56 in October 2002, P168,004.31 in November 2002, and P424,061.14 in December 2002. However, she could not show any proof of such purchases as they had already disposed the records of all their transactions for that period based on usual accounting practice.[29]

NIMFA A. MASCULINO, the Junior Bookkeeper of Asian Terminals, Inc. (ATI), alleged that per Official Receipt No. 104307 issued by petitioner to ATI on September 24, 2002, the latter purchased from petitioner during the fourth quarter of 2002 in the amount of P3,100.00. This receipt was part of a liquidation report submitted by ATI's former employees Mary

[28] Exhibit "Z".
[29] Exhibit "AA".

Jane dela Cruz and of ATI's accounting records in October 2002.[30]

ANNA MAY CEREDON, Liaison Officer of Lyncor, Inc. claimed that per Official Receipts Nos. 105485 and 106331,[31] their total purchases from petitioner for the fourth quarter of 2002 was only P30.00.[32]

LOIDA P. LEYSON, Accounting Officer of Shinsung Corporation, testified that Official Receipt No. 108629[33] indicates that on December 8, 2002, they purchased from petitioner, through Mr. So Young Lee Hong, in the amount of P1,929.00.[34]

On July 07, 2009, ***LOVELY MAGNAYE***, the Financial Reporting Manager of Jollibee Foods Corporation identified the Certification[35] she issued on April 3, 2007 to the effect that there were no sales made by petitioner to Jollibee Foods Corporation in the fourth quarter of 2002.

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[30] Exhibit "T".
[31] Exhibit "W-2".
[32] Exhibit "W".
[33] Exhibit "Y-2".
[34] Exhibit "Y".
[35] Exhibit "BB".

On August 20, 2009, petitioner rested its case and filed its Formal Offer of Evidence.

In a Resolution dated November 16, 2009, the Court admitted petitioner's Exhibits "F," "J," "K," "L," "M," "N," "O," "P," and "R" but denied the admission of the rest of the exhibits.

However, upon motion for reconsideration, the Court in the Resolution dated February 26, 2010, admitted petitioner's Exhibits "A," "B," "C," "D," "E," "G," "H," "I," "Q," "S," "T," "U," "X," "Y," "Z," "AA," and "BB."

Respondent, on the other hand, presented as its first witness, Evelyn R. Garces, Information Technology Officer I assigned at the Information System Development Service of the BIR National Office. She supervises the generation of reports regarding taxpayer's compliance, electronic submission of third party information, including Letter Notices. A Letter Notice is a computer generated document resulting from the automated matching of third party information on purchases with the VAT return filed by the taxpayer. The third party who is either a customer or a purchaser provides information about its transactions with the seller subject to VAT.

According to the witness, the generation of Letter Notices starts with the submission to the BIR of a summary list of purchases (SLP) by the customers/purchasers. Only those customers whose quarterly gross purchases exceed P1,000,000.00 are required to submit an SLP pursuant to Revenue Memorandum Order No. RMC 24-02 and Revenue Regulation 08-02. The SLP must be in a diskette for submission to the Revenue District Office (RDO) that has jurisdiction over the business *situs* on a quarterly basis. It shall be uploaded by the RDO to the Integrated Tax System (ITS) server that will electronically transmit the data to the Data Warehouse of the BIR. The encoded and uploaded VAT Returns filed by the seller with the BIR are likewise transmitted to the Data Warehouse.

Subsequently, a memorandum from respondent shall authorize the RDO to run the program that will match the SLP as declared by the customer with the sales per the seller's declaration. The same memorandum sets the threshold or percentage of the discrepancy/under-declaration between the purchases and sales that will merit the issuance of a Letter Notice. The computer program shall automatically compare the sales and purchases of each taxpayer and determine the discrepancies. If a discrepancy is detected, the computer program will determine if it matches with the threshold set in the system as indicated in the memorandum. If the discrepancies on the sales and purchases meet the set threshold, a Letter Notice together with a Quarterly Report on Third Party Information on Purchases will be automatically generated. The Letter Notice informs the taxpayer that the computerized matching of the purchases by their customers with the sales declared in their returns discloses a discrepancy/under-declaration. Thereafter, the taxpayer is invited to the Revenue District Office concerned to reconcile the apparent discrepancy.

There had been no complaints regarding the accuracy of the system for the past seven years of its implementation which started in the last quarter of 2002.

On cross-examination, the witness admitted that in 2002, she was not yet involved in the generation of reports from the BIR Integrated Tax System (ITS) that resulted in the issuance of the subject assessment. While there is a validation program provided by the BIR, such includes only the checking of the format of the file submitted and the viruses. The validation process does not include the checking of the substance or content of the SLP against any other source or documents.

Further, the SLP is only a listing without any attached invoices or receipt of the purchases stated in the said SLP.

The witness confirmed that the subject Quarterly Report on Third Party Information Purchases covers the fourth quarter of 2002 which was among the initial reports generated by the system when it was implemented in the last quarter of 2002. Since she does not handle tax assessments protests, she does not know if a complaint or protest has been filed by petitioner in relation to the discrepancies between the reports generated by the system and the actual sales, which is the basis of the subject assessment.

SAMIRA N. PAGDILAO, Revenue Officer III assigned at RDO No. 38, Quezon City, testified that she conducts audit examinations of taxpayers to determine their internal revenue tax liabilities and other matters referred to her by their group supervisor or revenue district officer.

Upon assignment and receipt of a Letter Notice, she notifies the taxpayer concerned to formally reply on the apparent discrepancies indicated in the Letter Notice. In the absence of the required explanation on the discrepancies noted, the BIR shall issue a Preliminary Assessment Notice (PAN). If the explanation to the PAN is still insufficient, a Formal Assessment Notice (FAN) is issued, otherwise, the case will be deemed closed and terminated.

In the instant case, the petitioner, through a Letter Notice, was informed about the discrepancies between the sales as shown in its tax return and the sales as reported by its customers. She served the Letter Notice to petitioner after it was assigned to her. When petitioner failed to file the requested reply, she served a second notice requiring petitioner to make a written reply lest the case would be referred to the legal division for appropriate action. Only then that it filed a reply. However, the said reply, coupled with supporting documents, did not sufficiently explain the discrepancies stated in the Letter Notice. Per her recommendation in a Memorandum[36] dated December 31, 2004, a PAN[37] with attached Details of Discrepancies was issued against petitioner. Since there was no protest timely filed, a FAN[38] was subsequently issued.

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[36] Exhibit "2".
[37] Exhibit "3".
[38] Exhibit "4".

Contrary to petitioner's contention, it received the FAN containing the computation of the assessed deficiency taxes as shown in the proof of receipt[39] appearing on the upper-right hand corner on the first page of the FAN. After receipt, petitioner filed a protest.

In both the PAN and the FAN, petitioner was subjected to deficiency IT based on the discrepancy amounting to P3,195,663.73 as revealed by petitioner's tax return and the sales reported by its customers. Such discrepancy is considered as undeclared sales. For respondent, the sources of funds not accounted in the taxpayer's returns leads to an adverse inference that part of taxpayers' income has not been reported. The discrepancies noted in the Letter Notice in the total amount of P3,195,663.73 was also subjected to VAT in both the PAN and the FAN as the discrepancy represents unreported sales. Under the Tax Code, all sales, unless otherwise exempt, are subject to VAT.

On cross, she claimed that she is familiar with the computer system that generated the Quarterly Report on Third Party Information which served as the basis of the subject

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[39] Exhibit "4-a".

deficiency assessment. The said Report was generated by the HEAD Office from the Summary Sales of Purchases submitted by the Top 10,000 Corporations. After the matching of the Report from the purchasers and the discovery of the discrepancies in the documents submitted by petitioner, the docket was assigned to the Districts, then to the RDO, who in turned, assigned the case to the examiner for verification.

The witness added that the Protest Letter of petitioner was filed on May 30, 2005, after the issuance of the FAN. Upon receipt of the Protest, the case was re-assigned to another examiner. Thus, she is not aware of the result of the said Protest.

After the testimony of its second witness, respondent filed her Formal Offer of Evidence on August 19, 2010.

In a Resolution dated September 22, 2010, the Court admitted all the documentary exhibits offered by respondent to which no objection was interposed by petitioner within the period granted. However, on September 24, 2010 or after the promulgation of the Resolution dated September 22, 2010, the Court received petitioner's Comment to respondent's Formal

Offer of Evidence which was filed through mail on September 7, 2010 or the last day for the filing of such pleading.

In a Resolution dated October 07, 2010, the Court noted petitioner' Comment but maintained its ruling to admit all of the documentary exhibits offered by respondent.

On November 25, 2010, petitioner filed its Memorandum. Respondent however failed to file any, despite notice.

In a Resolution dated December 06, 2010, the instant petition was submitted for decision.

The parties stipulated to submit the following issues for the resolution of the Court:[40]

> "1. Whether on 30 April 2005, petitioner received respondent's Formal Assessment Notice dated 28 April 2005 containing the exact amount of its deficiency tax liabilities, which is presently the subject matter of the petition;
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> 2. Whether petitioner has an undeclared income from its undeclared sales for the 4th quarter of 2002 in the amount of P3,195,633.73;

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[40] Stipulation of Issues, docket, p. 79.

3. Whether petitioner has filed its income tax return for the taxable year 2002 with Revenue District Office No. 50, South Makati;

4. Whether for the taxable year 2002, petitioner incurred the following tax liabilities: a) Deficiency Value-added tax covered by Assessment Notice No. VT-1136-02-05-0149 dated 28 April 2005 in the amount of P629,239.32; and b) Deficiency Income Tax covered by Assessment Notice No. IT-1136-02-05-0149 dated 28 April 2005 in the amount of P1,968,738.98;

5. Whether or not the reported purchases of alleged customers of petitioner for the fourth quarter of 2002, are valid and with basis."

The Ruling of the Court

On the face of the Petition for Review and the Answer thereto filed by respondent it is clear that the crux of the controversy lies on the validity and correctness of the assessment issued by respondent against petitioner. The disputed assessment based on the computer generated Quarterly Report on Third Party Information on Purchases is for the alleged unreported income from understatement of sales of petitioner during the fourth quarter of 2002 in the amount of P3,195,663.73 that was subjected to income tax in the amount of P1,968,738.98, and 10% VAT of P629,239.32, inclusive of surcharge and interest.

Be that as it may, the Court must first determine the timeliness of the filing of the instant Petition for Review which is intertwined with the first issue raised by the parties for the determination of the Court. In this regard, Section 228 of the National Internal Revenue Code (NIRC), as amended, is instructive, thus:

> "Section 228. **Protesting of Assessment. –** When the Commissioner or his duly authorized representative finds that proper taxes should be assessed, he shall first notify the taxpayer of his findings:
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> x x x x x x x x x
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> Such assessment may be protested administratively by filing a request for reconsideration or reinvestigation within thirty (30) days from receipt of the assessment in such form and manner as may be prescribed by implementing rules and regulations. Within sixty (60) days from filing of the protest, all relevant supporting documents shall have been submitted; otherwise, the assessment shall become final.
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> If the protest is denied in whole or in part, or is not acted upon within one hundred eighty (180) days from submission of documents, the taxpayer adversely affected by the decision or inaction may appeal to the Court of Tax Appeals within thirty (30) days from receipt of the said decision, or from the lapse of the one

> hundred eighty (180)-day period; otherwise, the decision shall become final, executory and demandable."

Evidence reveals that petitioner received the FAN dated April 28, 2005 with attached Details of Discrepancies two days from date of issue or on April 30, 2005,[41] assessing it for deficiency IT in the amount of P1,968,738.98 and deficiency VAT of P629,239.32 for the fourth quarter of 2002. The amounts were allegedly derived from undeclared income/discrepancy from sales of petitioner as reported by its clients/customers through their respective Quarterly Reports on Third Party Information on Purchases.

Aggrieved, petitioner filed its protest against the said assessment on May 30, 2005[42] in accordance with Section 228 of the NIRC, as amended. Per the parties' stipulation, petitioner submitted documents supporting its protest on July 29, 2005,[43] which was well within the 60-day period mandated in Section 228 of the same Code.

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[41] Exhibits "4" and "4-a".
[42] Exhibit "B" and "7".
[43] Par. 1, Stipulation of Facts, Joint Stipulation of Facts filed on July 27, 2006, docket p. 78.

Respondent however, failed to act on the said protest within the allowable period of 180 days which lapsed on January 25, 2006.[44] From the said date, petitioner had 30 days to assail such inaction of respondent before the Court. Thus, petitioner timely filed the instant Petition for Review on February 24, 2006.

On the issue of whether petitioner filed its Income Tax Return (ITR) for the taxable year 2002 with Revenue District Office No. 50, South Makati, suffice it to say that neither of the parties dwelled nor gave premium on it. No evidence - testimonial or documentary - was presented on the matter thereby precluding the Court from making any finding of fact that would justify a ruling on the matter. Besides, the issue is of no moment as the alleged undeclared sales were allegedly derived from third party information compared with the VAT return for the 4th quarter of 2002 and its supporting documents submitted by petitioner. In fact, respondent, who is in custody of all documents submitted by all taxpayers including petitioner, did not find it relevant to merit its presentation in Court.

On the validity and veracity of the assessment for the alleged undeclared income from petitioner's unreported sales for

[44] Par. 2, Stipulation of Facts, Joint Stipulation of Facts filed on July 27, 2006, docket p. 78.

the 4th quarter of 2002 in the amount of P3,195,633.73, note that the subject assessment is based on the electronically generated document known as Quarterly Report on third Party Information on Purchases.[45] It summarized petitioner's alleged undeclared sales as follows:[46]

Per Summary List of Purchases submitted by your customers	P 5,007,571.73
Sales per Tax Return of petitioner	1,811,908.00
Discrepancy in Sales (under-declaration)	**P 3,195,663.73**
Percentage (%) of Discrepancy	63.82%

The foregoing purported sales to petitioner's customers are as well reflected in the Quarterly Report, as follows:

		Gross Taxable Purchases	
Name of Purchaser	**Year 2002**	**For the Month**	**For the Quarter**
SM Mart, Inc.	October	P 555,365.30	
	November	574,387.60	
	December	1,306,326.70	P 2,436,079.60
Manila Southern Associates, Inc.	October	P 104,809.20	
	November	93,603.20	
	December	233,456.50	431,868.90
Major Shopping Management Corp.	October	P 237,906.40	
	November	182,065.20	
	December	323,099.50	743,071.10
Plaza Arcade Inc.	October	P 87,863.56	
	November	168,004.31	
	December	424,061.14	679,929.01

[45] Exhibit 1-b.
[46] Exhibits "1", "1-b", and "1-b-1".

Multi Store Corporation	October	P 107,390.90	
	November	121,511.00	
	December	238,253.10	467,155.00
Mercantile Stores Group, Inc.	October	P 50,815.60	
	November	67,498.30	
	December	119,559.90	237,873.80
Asian Terminals Inc.	October		2,818.20
Cornell Foods Inc.	October		409.09
Edsa Shangri-La Manila	October		727.30
Hi-Integra Inc.	October		49.09
Jollibee Foods Corp.	October		537.90
Oriental Pasta, Inc.	October	P 69.60	
	December	55.23	124.83
Sports Grill Phils. Inc.	October	P 1,165.45	
	November	2,383.64	3,549.09
Student's Chow Place Corp.	October		350.00
Arancia, Inc.	November		88.64
Chongson John Christopher PE	November		68.18
Leisure and Allied Indust Phils Inc.	November	P 118.60	
	December	290.95	409.55
Lyncor Inc.	November	P 13.64	
	December	13.64	27.28
Prime Colors International Inc.	November		71.60
Semicon Inc.	November		342.72
ABS CBN Broadcasting Corp.	December		27.30
Greasebee Auto Care Center Inc.	December		190.91
Music One Corporation	December		49.00
Shinsung Corporation	December		1,753.64
			P 5,007,571.73

Respondent claims that these sales were reported to the BIR by the very purchasers of petitioner through their respective Summary Lists of Purchases submitted pursuant to Section

4.110-4 of Revenue Regulations No. 7-95, as amended by Revenue Regulations No. 13-97 and Revenue Regulations No. 7-99.

However, when served with Subpoenas Duces Tecum and Subpoenas Ad Testificatum,[47] eleven (11) of the fifteen (15) alleged purchasers of petitioner, through their duly authorized officers or representative, either controverted or denied respondent's allegations, as follows:

Reference	**Document**	**Third Party**	**Statement**
Exh. Z	Judicial Affidavit	SM Mart, Inc.	**No purchases** of goods or services from petitioner for the 4th quarter of 2002
Exh. BB	Certification	Jollibee Foods Corporation	**No transactions** with petitioner in the 4th quarter of 2002
Exh. Q	Judicial Affidavit	Leisure and Allied Industries Phils., Inc.	total purchases from petitioner for the 4th quarter of 2002 is **P623.75**, with ORs
Docket, p. 261	Ex-Parte Manifestation	ABS-CBN Broadcasting Corporation	**No document or receipt** showing it has entered into a transaction with petitioner
Exh. U	Affidavit	Arancia, Inc.	**No transactions** with petitioner in the 4th quarter of 2002
Exh. T	Sworn Statement	Asian Terminals, Inc.	total purchases from petitioner for the 4th quarter of 2002 is **P3,100.00**, with OR
Exh. V	Judicial Affidavit	Music One Corporation	**Never purchased** from petitioner during the 4th

[47] Docket, pp. 178-181.

			quarter Of 2002
Exh. W and W-2	Judicial Affidavit	Lyncor, Inc.	Total purchases from petitioner for the 4th quarter of 2002 is **P30.00**, with Ors
Exh. X	Judicial Affidavit	Hi-Integra, Inc.	**No purchases** of goods or services from petitioner for the 4th quarter of 2002
Exh. Y and Y-2	Judicial Affidavit	Shinsung Corporation	Total purchases from petitioner for the 4th quarter of 2002 is **P1,929.00**, with OR
Exh. AA	Judicial Affidavit	Plaza Arcade, Inc.	**No proof of purchases** since records were already disposed

Up against the foregoing testimonies of the third party purchasers is the Quarterly Report of the BIR which shows considerable discrepancies, to wit:

Third Party	**Actual purchases made by third party for the 4th quarter of 2002**	**Sales of petitioner per Quarterly Report, Net of VAT**
SM Mart, Inc.	none	P 2,436,079.60
Jollibee Foods Corporation	none	537.90
Leisure and Allied Industries Phils., Inc.	P623.75 (inclusive of VAT of P56.70, with Ors)	409.55
ABS-CBN Broadcasting Corporation	none	27.30
Arancia, Inc.	none	88.64
Asian Terminals, Inc.	P3,100.00 (inclusive of VAT of P281.80, with OR)	2,818.20
Music One Corporation	none	49.00
Lyncor, Inc.	P30.00	27.28

	(inclusive of VAT of P2.72, with ORs)	
Hi-Integra, Inc.	none	49.09
Shinsung Corporation	P1,929.00 (inclusive of VAT of P175.36, with OR)	1,753.64
Plaza Arcade, Inc.	none record disposed	679,929.01
TOTAL	**P 5,682.00**	**P 3,121,769.21**

From the foregoing table, the total purchases made by the third party purchasers from petitioner for the 4th quarter of 2002, based on their own records/documents and books of account is only P5,682.00. On the other hand, based on the BIR Quarterly Report for the same details, it is P3,121,769.21. Significantly and as admitted by respondent's own witness Evelyn R. Garces, the summary lists of purchases received by the BIR were not verified with other externally sourced data to check the integrity of the information gathered. In fact, she categorically testified that Integrated Tax System of the BIR can only check or validate the format and possible viruses in the computer program but certainly not the content or substance of the encoded summary lists of purchases. She declared as follows:

> "Atty. Calibo
> Q: When purchasers submit this Summary List of Purchasers as you mentioned in your Affidavit, do you verify

this data that they present to you before you upload it to the system or do you merely take the data that they give to you and upload it directly to the system without any verification or comparison with any source of information?

Ms. Garces
A: As far as I remember, when the BIR release (sic) this regulation, it states there that there is an RNC where in a specified format for the Summary List of Purchases or Sales, there is a validation program provided by the BIR so we required all the taxpayers submitting their SLS or the SNT that this data should undergo validation before it is uploaded to our server.

Atty. Calibo
Q: How does this validation, how is this performed, this validation process?

Ms. Garces
A: It's also computer, (sic) Sir, system.

Atty. Calibo
Q: Okay, my question is, I understand when you referring (sic) to RNC for 2006 customer and submit with the BIR this List of Purchases in Excel Format. Am I correct?

Ms. Garces
A: Yes.

Atty. Calibo
Q: Now for instance, if you received a file or a soft copy of this document in Excel Format, do you upload it directly to your system?

Ms. Garces
A: No. the file undergoes to (sic) validation.

Atty. Calibo
Q: Can you please describe how is this validation process work? (sic)

Ms. Garces
A: It checks the conformity of the file, it checks for viruses.

Atty. Calibo
Q: But it does not check the correctness of the values in the file against any other source of information? Meaning, your (sic) checking with respect to the format but not the substance of that file. Am I correct?

Ms. Garces
A: Yes.

Justice Uy
Can I just ask a follow-up question on this matter? So, when a list is submitted, is the purchaser or the customer required to attach the document evidencing the transaction like for a sale, do they attach the invoice or just merely a listing (interrupted)

Ms. Garces
It's just merely the listing, your Honors.

Justice Uy
Listing?

Ms. Garces
Yes, your Honors.

Justice Uy
So, there is no way to verify whether that sale did really occur, it's just a list?

Ms. Garces
Yes, your Honors."[48]

Incidentally, this witness admitted that she was not the one who caused neither has she any participation in the

[48] Transcript of Stenographic Notes dated May 18, 2010, pages 28-32.

generation of the subject Quarterly Report, which became the basis of the disputed assessment. In fine, she has no competence to testify on the subject document.

While it is true that tax assessments have the presumption of correctness and regularity in its favor, it is also equally true that assessments should not be based on mere presumptions no matter how reasonable or logical the presumption might be. This was highlighted in the case of *Commissioner of Internal Revenue vs. Hantex Trading,*[49] the pertinent portion of which is quoted below as follows:

> "We agree with the contention of the petitioner that, as a general rule, 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. It is to be presumed, however, that such assessment was based on sufficient evidence. Upon the introduction of the assessment in evidence, a *prima facie* case of liability on the part of the taxpayer is made. If a taxpayer files a petition for review in the CTA and assails the assessment, the *prima facie* presumption is that the assessment made by the BIR is correct, and that in preparing the same, the BIR personnel regularly performed their duties. This rule for tax initiated suits is premised on several factors other than the

[49] G.R. No. 136975, March 31, 2005.

> normal evidentiary rule imposing proof obligation on the petitioner-taxpayer: the presumption of administrative regularity; the likelihood that the taxpayer will have access to the relevant information; and the desirability of bolstering the record-keeping requirements of the NIRC.
>
> However, the *prima facie* correctness of a tax assessment does not apply upon proof that an assessment is utterly without foundation, meaning it is arbitrary and capricious. Where the BIR has come out with a "naked assessment," *i.e.*, without any foundation character, the determination of the tax due is without rational basis. In such a situation, the U.S. Court of Appeals ruled that the determination of the Commissioner contained in a deficiency notice disappears. *Hence, the determination by the CTA must rest on all the evidence introduced and its ultimate determination must find support in credible evidence.*

Finally, the imputation of fraud against petitioner adding 50% surcharge to its alleged income and value-added tax liabilities, cannot hold water since the claimed fraudulent intent was merely deduced from the fact that there was an under-declaration of sales and/or income for the 4th quarter of 2002, which she utterly failed to establish. Since the under-declaration was found to be inexistent, there is no basis for the allegation of fraud justifying the imposition of 50% surcharge against petitioner. Settled is the rule that fraud cannot be presumed but must be proved.[50]

In the case of *Wintelecom, Inc. vs. Commissioner of Internal Revenue*[51], this Court held, thus:

> "**Considering the enormous power given to respondent and the leniency in the kinds of evidence respondent may accept as basis for his assessments, he had no excuse in failing to present to this Court the third party information on which the BIR examiners based the assessments.** It must not be forgotten that an assessment must be based on actual facts. For his failure to support his allegation as regards the third party information, the assessment for deficiency income taxes for years 2001 and 2000 xxx is cancelled for lack of basis. **As for the imposition of the fifty percent (50%) civil penalty, the same is moot since there is no assessment to speak of.**" (*Emphasis supplied*)

WHEREFORE, the instant Petition for Review filed by petitioner Fax N Parcel, Inc. is hereby **GRANTED**. Accordingly, the deficiency income tax and VAT assessments in the aggregate

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[50] *Aznar v. Court of Tax Appeals, et al.*, G.R. No. L-20569, August 23, 1974.
[51] CTA Case No. 7056, February 20, 2008.

amount of P3,195,663.73 are hereby cancelled and withdrawn, for lack of factual basis.

SO ORDERED.

ESPERANZA R. FABON-VICTORINO
Associate Justice

We concur:

ERNESTO D. ACOSTA
Presiding Justice

ON LEAVE
ERLINDA P. UY
Associate Justice

CERTIFICATION

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

ERNESTO D. ACOSTA
Presiding Justice