# REPUBLIC OF THE PHILIPPINES
# COURT OF TAX APPEALS
# QUEZON CITY

**AUSTRALASIA CYLINDER CORPORATION,**
Petitioner,

- versus -

**COMMISSIONER OF INTERNAL REVENUE,**
Respondent.

C.T.A. CASE NO. 6014

Promulgated:

AUG 14 2002

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## DECISION

This is an assessment case involving deficiency income tax for the year 1995 in the total amount of P2,399,488.14.

Petitioner is a domestic corporation engaged in the manufacture of steel drums and liquid petroleum gas cylinders.

Petitioner's books of accounts were examined by the Revenue District Office at Novaliches, after which, petitioner was issued deficiency assessment for income tax amounting to P27,000.00 including increments that it promptly paid (*Joint Stipulation of Facts, par. 3*).

The examination docket was forwarded to the Regional Assessment Division of the respondent's Revenue Region No. 7 in Quezon City for review and clearance by the Regional Assessment Division which instead issued the subject final assessment notice (*No. 000026 dated April 13, 1999*) and demand letter (*No. 2860*) to petitioner for alleged income tax deficiency for 1995 (*Joint Stipulation of Facts, par. 4; Exhibits A& B; Exhibit 5*).

Petitioner protested the assessment on May 20, 1999 (*Exhibit C*) and thereafter transmitted the necessary documents on July 19, 1999 (*Joint Stipulation of Facts, par. 5*). Allegedly included in said transmittal letter (*Exhibit E*) were the relevant supporting documents to bolster its arguments in overturning the assessment rendered.

Claiming inaction by the respondent on the protest, petitioner filed the instant petition on February 14, 2000.

For determination by this court are the following issues:

(1) Whether or not the person who issued the assessment notice has authority to do so;

(2) Whether or not the assessment notice is void for failure to inform petitioner of the law and the facts on which it was made; and

(3) Whether or not the disallowance made by the respondent on petitioner's claimed tax credits is proper.

Petitioner mainly based its judicial appeal on Section 228 of the 1997 Tax Code, partly quoted, as follows:

> **SEC. 228. *Protesting of Assessment.*** – When the Commissioner or his duly authorized representative finds that proper taxes should be assessed, he shall first notify the taxpayer of his findings: *Provided, however*, That a pre-assessment notice shall not be required in the following cases:
>
> xxx xxx xxx
>
> The taxpayers shall be informed in writing of the law and the facts on which the assessment is made; otherwise, the assessment shall be void.

Within a period to be prescribed by implementing rules and regulations, the taxpayer shall be required to respond to said notice. If the taxpayer fails to respond, the Commissioner or his duly authorized representative shall issue an assessment based on his findings.

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.

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."

Respondent, for his part, raised the following Special and Affirmative Defenses, to wit:

"5. Section 228 of the National Internal Revenue Code, indeed, specifically requires that the taxpayer (Petitioner herein) be informed in writing of the law and the facts on which the assessment is made. However, the said Article of the National Internal Revenue Code does not specifically require that the law and the facts from which the assessment was made be embodied in the Assessment Notice itself. Attached to the assessment notice was the Demand Letter issued by the Assessment Division of BIR Revenue Region No. 7 through its Division Chief, Mrs. Ruth Vivian G. Gadia. The Demand Letter issued by the Assessment Division against the herein Petitioner has sufficiently provided for the Respondent's basis in issuing the assessment against the Petitioner. Thus, the mandatory requirement set forth in Section 228 of the National Internal Revenue Code has been sufficiently complied with. Consequently, the assessment issued against the Petitioner cannot be said to be void *ab initio*.

6. Section 6 of the 1997 National Internal Revenue Code is the appropriate law governing the power of the Commissioner of Internal Revenue to make examinations of taxpayer's books and other accounting records as well as the power to issue assessments against the taxpayer. Under the said provision of the National Internal Revenue Code, the Commissioner of Internal Revenue may delegate the power

vested in him by Section 6 of the Tax Code to his authorized representative. With regard to the issuance of Assessment Notices, the appropriate person designated by the Commissioner of Internal Revenue to perform such task is the Chief of Assessment Division of the Revenue Region which has jurisdiction over the taxpayer. In the instant case, Mrs. Ruth Vivian G. Gadia, the Chief of the Assessment Division of Revenue Region No. 7 is the authorized representative of the Commissioner of Internal Revenue who is vested with the power to issue the Assessment Notice against the taxpayer. Section 6 of the National Internal Revenue Code is hereunder quoted to read:

> **Section 6.** ***Power of the Commissioner to Make Assessments and Prescribe Additional Requirements for Tax Administration and Enforcement. –***
>
> (a) Examination of Returns and Determination of Tax Due. – After a return has been filed as required under the provisions of this Code, <u>the Commissioner or his duly authorized representative</u> may authorize the examination of any taxpayer and the assessment of the correct amount of tax: Provided, however, That failure to file a return shall not prevent the Commissioner from authorizing the examination of any taxpayer.
>
> <u>The tax or any deficiency tax so assessed shall be paid upon notice and demand from the Commissioner or from his duly authorized representative.</u> (Underscoring Supplied)

7. The assessment was issued in accordance with law and regulations; and

8. All presumptions are in favor of the correctness of tax assessments. **(Commissioner of Internal Revenue vs. Avelino, 8 SCRA 572)**"

We deal first with the issue of whether or not the person who issued the assessment notice has authority to do so. After all, if the person issuing the assessment has no authority to do so, then the assessment is void *ab initio*.

Petitioner argues that the person issuing the assessment, *i.e.*, the Chief of the Assessment Division, Revenue Region No. 7 in this case, has no legal authority to do so. Consequently, the assessment is procedurally and substantially defective, thus invalid.

Petitioner argues that the pertinent provision is Section 10 of the Tax Code, as amended, partly quoted, *viz*:

> **SEC. 10.** *Revenue Regional Director.* – Under rules and regulations, policies and standards formulated by the Commissioner, with the approval of the Secretary of Finance, the Revenue Regional Director shall, within the region and district offices under his jurisdiction, among others:
>
> (a) Implement laws, policies, plans, programs, rules and regulations of the department or agencies in the regional area;
>
> (b) Administer and enforce internal revenue laws, and rules and regulations, including the assessment and collection of all internal revenue taxes, charges and fees.

On the other hand, respondent posits that the applicable provision is Section 6 of the Tax Code, as amended. Under the said provision, the Commissioner may delegate the powers to make assessments and prescribe additional requirements for tax administration and enforcement. With regard to the issuance of assessment notices, the appropriate person to perform such task is the Chief of the Division of the Revenue Region concerned.

We concur with the respondent on this point. Section 6(A) of the 1997 Tax Code provides in pertinent part:

> "**SEC. 6.** *Power of the Commissioner to Make Assessments and Prescribe Additional Requirements for Tax Administration and Enforcement*
>
> "(A) Examination *of Returns and Determination of Tax Due.* – After a return has been filed as required under the provisions of this Code, the Commissioner or his duly authorized representative may authorize the examination of any taxpayer and the assessment of the correct amount of tax:

> *Provided, however,* That failure to file a return shall not prevent the Commissioner from authorizing the examination of any taxpayer.
>
> "The tax or any deficiency tax so assessed shall be paid upon notice and demand from the Commissioner or from his duly authorized representative.
>
> " x x x." [Underscoring supplied.]

Section 6 clearly provides that the Commissioner of Internal Revenue or his duly authorized representative may authorize the assessment of taxpayers for deficiency tax. We believe that the person who signed the assessment notice here for the Commissioner of Internal Revenue, namely, Ms. Ruth Vivian G. Gadia, the Chief, Assessment Division, Revenue Region No. 7 of the Bureau of Internal Revenue, is the duly authorized representative of the Commissioner. After all, there is the presumption of regularity in the exercise of official functions coupled with the fact that respondent Commissioner of Internal Revenue himself affirms that the said revenue official is duly authorized to do so in this case.

The Supreme Court had the occasion to rule that a person signing in behalf of the then Collector (now Commissioner) of Internal Revenue is authorized to issue an assessment even if his position is unrevealed and even if he did not state his authority to sign for his chief. In *Collector of Internal Revenue vs. Bohol Land Transportation Co.*, G.R. Nos. L-13099 and L-13462, April 29, 1960, 107 Phil. 965, the Supreme Court held:

> The company argues that its failure to substantiate its defense insofar as the years 1945 to 1950 are concerned should not be held against it for there is no validity to the *prima facie* correctness of the Collector's findings since the assessments are signed not by the Collector, nor by the chief of income tax division, but by one Casto Ayeras, who did not even reveal his position, nor state if he had any authority to sign for his chief. This contention is untenable, for a cursory examination of the assessment notices will show that they were duly signed by Ayeras in behalf of his chief, the Collector. Under the set-up of

> the Bureau of Internal Revenue, the chief of the income tax division as regards tax assessments is possessed of delegated powers to issue assessment notices in behalf of the Collector of Internal Revenue. And in such a case, we may not infer that the decision is not the decision of the Collector himself.

We cannot give credence to petitioner's argument that Section 10 of the Tax Code limits the delegated authority to issue assessments only to the Revenue Regional Director of the region concerned. There is nothing in the aforementioned Section that expressly or impliedly so states. Stated otherwise, Section 10 of the Tax Code does not limit the term "duly authorized representative" under Section 6 of the same Code to the Revenue Regional Director of the region concerned for the purpose of issuing assessments. At most, it merely recognizes that said Regional Director is a duly authorized representative as opposed to being the sole authorized representative of the Commissioner.

In the absence of any clear repudiation of authority by respondent Commissioner of Internal Revenue, we conclude that Ms. Ruth Vivian G. Gadia, the Chief, Assessment Division, Revenue Region No. 7 of the Bureau of Internal Revenue, was duly authorized to issue the assessment in question.

The second issue raised herein is whether or not the assessment notice is void for failure to inform the petitioner of the law and the facts on which the assessment is made. The third issue involves the question of the propriety of respondent's disallowance of petitioner's claimed tax credits. These issues are deeply intertwined in this case so they are being resolved jointly.

Respondent posits that although Section 228 of the Tax Code, as amended, specifically requires that the taxpayer be informed in writing of the law and the facts on which the assessment is made, the same article does not specifically require that the law and the facts on which the assessment was made be embodied in the assessment notice itself.

We agree. In whatever manner and form the assessment notice is written, as long as the taxpayer is informed on how the assessment was arrived at, then the requirement of said law is sufficiently met.

Respondent thus asserts that the demand letter (*Exhibit B*) attached to the assessment notice (*Exhibit A*) contains the necessary information on how the assessment came about.

We beg to differ. The demand letter was devoid of factual as well as legal bases that would enlighten anyone, this court included, on how and why the assessment was reached. The computation made by the respondent lacked any support and did not state the basis either in fact or in law for the disallowances made. To explicitly illustrate, said demand letter is hereby reproduced:

| | | |
|---|---|---|
| Net income per Investigation | | P3,121,556.49 |
| Add: Audit Findings/Discrepancies Per Review | | |
| Net Income Per Review | | 3,121,556.49 |
| Income Tax Due Thereon | | 1,092,544.77 |
| Less: Tax Credits | | |
| Tax paid | 331,034.86 | |
| Other payment per Investigation | 27,000.00 | 358,034.86 |
| Tax Credit forwarded to succeeding Quarter | | 776,671.36 |
| DEFICIENCY TAX | | 1,501,181.27 |
| Interest | | 898,306.87 |
| TOTAL AMOUNT DUE AND COLLECTIBLE (excluding increments) | | P2,399,488.14 |

The demand letter did not expound on how the respondent arrived at the taxable income per investigation of P3,121,556.49. Nor did it provide for the details of the difference between petitioner's net income of P853,924.31 as reported in the 1995 income tax return (*Exhibits F; 1*) and the said net income per investigation or what were added up by the examiners to the audited net income to come up with the net income per return/investigation. In fact, it was clearly indicated in the demand letter that there were no audit findings/or discrepancies per review. Neither did the assessment notice nor the demand letter explain why the total tax credits of P776,671.36 was not recognized by the respondent. In the hearing of January 29, 2001, respondent's witness testified that in the absence of photocopies of certificates of creditable income tax withheld at source, the creditable taxes amounting to P734,509.91 were being disallowed (*TSN, page 17*). This amount was the difference between the income tax due of P1,092,544.77 and the payments credited totaling P358,034.86 (P331,034.86 per quarterly ITR and P27,000.00 per investigation). If that was the only reason for the disallowance thereof, it may be worth mentioning that petitioner was able to present as part of its evidence, the subject certificates of creditable income taxes withheld at source (*Exhibits K, L, M, N, O, P and Q*).

Still, that is beside the point. Based on the demand letter, respondent disallowed the tax credits forwarded to the succeeding quarter of 1995 amounting to P766,671.36 without giving reasons therefor. However, during the hearing of the case on the merits, respondent's witness explained that BIR Form No. 1702 (Revised: January 1995) partly provided that:

> TAX REFUND OR CREDIT –
>
> An excess of the total tax credits/payments over the actual income tax computed in the final income tax return may be refunded to the taxpayer or credited against his estimated income tax liabilities for the quarters of the succeeding taxable year. The taxpayer shall exercise his option by checking

the appropriate box. In case the taxpayer fails to signify his choice, the excess payment shall be automatically credited.

Inasmuch as the taxpayer-petitioner did not indicate nor mark its intention whether to claim for a refund or apply the excess payments as tax credits to the succeeding year, the usual procedure followed by the BIR was adopted i.e., to apply the excess payments as tax credits to the succeeding year (*TSN, July 11, 2001, pages 6 & 7*). By following said process, the tax credits of P766,671.36 were deducted from the total reported tax credits/payments and could not be utilized to pay off taxpayer's income tax liability for the period (*ibid, pages 8 & 9*). In short, respondent presumed that the said excess tax payments for 1995 were carried over to 1996 and applied against its tax liability for the said year. Thus, the deficiency income tax due in 1995 should not be applied against the tax credit of P766,671.36 (*See TSN, January 29, 2001, pages 17 & 23*). If that should be the rule, respondent should not have added up the same amount in computing petitioner's tax liability for 1995 (*See Exhibit B*).

But it must be observed that the aforequoted provision refers to "excess" tax credits. Applying the same provision in the case at bar, petitioner's tax due of P298,873.51 reported in its income tax return should first be deducted from its total tax credits/payments for the year in the amount of P766,671.36. The principle of automatic crediting should apply only to the excess tax credits/payments and not to the total tax credits declared for the year as propounded by the respondent.

Anent the other disallowances, the BIR Revenue Officer testified that they pertained to several expenses, namely: insurance expense, security services, miscellaneous expense, donations and contributions, transportation and travel, rental, delivery expenses, repair and maintenance, in the total amount of P2,267,633.80 (*TSN, January 29, 2001, page 11*). Hence, the discrepancy in the allowable deductions as per income tax return and allowable deductions as per audit. Ostensibly, the disallowed expenses of P2,267,632.80 were added to petitioner's taxable income of P853,924.31 thereby increasing petitioner's taxable income to P3,121,556.49 (*TSN, January 29, 2001, page 16*). The amount of P3,121,556.49 was then multiplied by 35%, the corporate tax rate arriving at the basic tax due of petitioner of P1,092,544.77 (*TSN January 29, 2001, page 22*).

It must be pointed out that disallowances made by the respondent appeared to be valid and proper. In fact, petitioner did not controvert the same. It willingly paid the tax due from said discrepancy in the amount of P27,000.00 (*id., page 15; Joint Stipulation of Facts, par. 3*). This was computed by subtracting the increased tax due of petitioner per investigation of P1,092,544.7 by P1,065,544.77, the declared total tax credits/payments for 1995.

Nonetheless, whatever explanations respondent's witnesses have relative to the subject assessment is inconsequential. The crucial point is the act of informing petitioner in writing on why were such disallowances made or why were petitioner's tax credits disallowed resulting to the subject assessment. Both the assessment notice (*Exhibit A*) and demand letter (*Exhibit B*) gave petitioner no inkling on how the assessment was arrived at, which is in direct violation of Section 228 of the Tax Code, as amended.

**IN VIEW OF ALL THE FOREGOING**, the instant petition is hereby **GRANTED**. Assessment Notice No. 000026 issued against petitioner for deficiency income tax covering the year 1995 in the amount of P2,399,488.14 is accordingly **CANCELLED** and **SET ASIDE**.

**SO ORDERED.**

Juanito C. Castañeda, Jr.
**JUANITO C. CASTAÑEDA, JR.**
Associate Judge

**I CONCUR:**

**ERNESTO D. ACOSTA**
Presiding Judge

## CERTIFICATION

I hereby certify that the above decision was reached after due consultation with the members of the Court of Tax Appeals in accordance with Section 13, Article VIII of the Constitution.

**ERNESTO D. ACOSTA**
Presiding Judge