REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

EDWARD POTENCIANO,
Petitioner,

- versus -

C.T.A. CASE NO. 4128

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:
FEB 20 1995

x - x

D E C I S I O N

This is a petition for review of the decision of respondent Commissioner of Internal Revenue dated November 11, 1986, holding petitioner liable for alleged deficiency income tax and penalties in the amount of P1,332,431.87 and deficiency percentage tax and penalties in the amount of P503,702.00 for the taxable year 1979.

Petitioner was the proprietor of a NACIDA registered metalcraft business under the business style of "Mccoy Metalcraft" registered in 1979, besides running a small tailoring/dress shop located in Binan, Laguna. Sometime in 1984, petitioner was subjected to an investigation by the Bureau of Internal Revenue in San Pablo City under Letter of Authority No. 0073779 dated May 24, 1984. As a result of said investigation, petitioner was assessed the aforementioned deficiency income and percentage taxes and penalties for 1979, which assessment was received by him on February 11, 1985. On March 1, 1985, said assessment was formally protested by petitioner through counsel in a letter dated February 26, 1985. On December 8, 1986, he received a letter from the Commissioner of Internal Revenue dated November 11, 1986 reiterating the demand for payment of the said deficiency taxes in the amounts of P1,332,431.87 and P503,712.00, thus, in effect, denying petitioner's administrative protest. Hence, this appeal by way of petition for review filed with this Court on January 6, 1987.

The aforesaid facts are recited in the body of the petition for review under the heading "jurisdictional allegations" and are admitted by the respondent in his answer.

In his petition, petitioner argues that respondent has no legal, factual and equitable basis for assessing the subject deficiency income and percentage taxes as the imputation by respondent of petitioner's annual gross sales amounting to P1,400,000.00 for the year in question was not based on actual and verified volume of business done for the year but was simply arrived at on the basis of mere conjecture or speculation, if not extrapolation of respondent's revenue examiner. Petitioner alleges that he was not a manufacturer subject to 10% manufacturer's sales tax as contemplated by Section 199 of the Tax Code. On the contrary, his metalcraft business was a tax exempt entity engaged in cottage industry registered under the NACIDA Law and had not exceeded the volume limit prescribed by said law which would warrant the losing of its tax exempt status. Moreover, petitioner asserts that respondent's right to assess the deficiency taxes in question has already prescribed; that the alleged sale of property by T.H. Quimio to petitioner was never consummated; and that petitioner did not actually receive any rental income that could be subject to income tax; and lastly, that petitioner has availed of the tax amnesty under Executive Order No. 41.

Respondent, for his part, denies all the above allegations of petitioner and, by way of special and affirmative defenses, alleged that the subject assessments were arrived at after a BIR examiner's investigation and finding that petitioner had manufactured passenger jeepneys as principal product for the year in question and sold an average of two (2) units of jeepney per month with an estimated cost of P60,000.00 per unit or a yearly gross sales of P1,440,000.00. Accordingly, assessments for deficiency percentage and income taxes were issued as follows:

COMPUTATION OF DEFICIENCY BUSINESS TAX FOR YEAR 1979

Gross Receipt (Metalcraft)	P1,440,000.00
10% Tax Due Thereon	P 144,000.00
Less: Tax Credits/Payments Made	-
Deficiency Sales Tax	P 144,000.00
Add: 50% Fraud penalty	72,000.00
25% Surcharge	54,000.00
14% Interest 4-20-79 to 7-31-80 (26.56%)	71,712.00
20% Interest 8-01-80 to 10-23-84 (60%)	P 162,000.00
TOTAL AMOUNT DUE & COLLECTIBLE	503,712.00

COMPUTATION OF DEFICIENCY INCOME TAX FOR THE YEAR 1979

Net income per return		P 18,505.81
Add:		
1. Unexplained source of income	243,451.19	
2. Unreported income from sale of 24 units of passenger jeepneys	1,440,000.00	1,683,451.19
Net Income per investigation		1,701,957.00
Less: Exemptions		6,000.00
Net Taxable Income		1,695,957.00
Tax Due Thereon		P 540,759.95
Less: Paid per return		1,292.00

Deficiency Income Tax	P 539,467.95
Add: 50% Fraud penalty	269,733.97
14% Interest 4-16-80 to 7-31-80 (4.66%)	
20% Interest 7-31-80 to 10-23-84 (60%)	485,521.15
TOTAL AMOUNT DUE & COLLECTIBLE	P1,332,431.87

NOTE; -

Purchase of Commercial building (Refer to Exh. 2) ---		P400,000.00
Cash on hand as of Dec. 31, 1979 ---	16,548.81	
Loans Payable - PNB -	140,000.00	156,548.81
UNEXPLAINED SOURCE OF INCOME		P243,451.19

Respondent also argues that his right to assess and collect the instant deficiency taxes has not yet prescribed; that the 50% fraud penalty was imposed due to substantial underdeclaration of income by the petitioner and that the assessment was issued in accordance with law.

The relevant issues for resolution by the court are as follows:

(1) Whether or not the right of respondent to assess the deficiency income and percentage taxes in question has already prescribed;

(2) Whether or not the availment of the tax amnesty by the petitioner would relieve it of the said deficiency taxes assessed by respondent;

(3) Whether or not the deficiency assessment has factual and legal basis;

(4) Whether or not the petitioner may be classified as a manufacturer and may no longer qualify as a tax-exempt person or entity under the NACIDA Law;

(5) Whether or not the imposition of the 50% fraud penalty is correct.

On the first issue, the facts of the case are clear. The income tax return of petitioner was filed on April 15, 1980 and the assessment was received by petitioner's counsel on February 11, 1985. Therefore, the five-year prescriptive period then provided under Section 318 of the Tax Code (effective in 1979) has not yet prescribed, counted from the filing of petitioner's return on April 15, 1980. On the other hand, for purposes of the percentage tax, petitioner failed to show that he has filed the corresponding business tax return. Moreover, per the BIR records, petitioner had executed a waiver of the statute of limitations prescribed pursuant to the National Internal Revenue Code (p. 232, BIR records).

As regards the second issue, this court finds the availment of the tax amnesty under Executive order No. 41 as not valid insofar as the subject assessment is concerned because petitioner is disqualified under Section 4(e) of the said Executive Order, more particularly relative to the inhibitions therein stating:

"those with tax cases pending investigation by the Bureau of Internal Revenue arising from valid information furnished under Section 316 of the Tax Code, as amended". The BIR records (pages 76 and 91) show that the tax investigation was precipitated by an information furnished the Bureau of Internal Revenue by Danilo Garcia, Dr. Ruben Yatco, Lucila Mondez and Lilia Alcantara on the 28th of October, 1983 and 12th of March 1984 for purposes of claiming the informer's reward under Section 316 of the Tax Code and under Republic Act No. 2338.

Having ruled that the assessment is not yet barred by prescription and that the petitioner is disqualified from availing the tax amnesty in relation to the subject assessments, we shall now come to the third issue.

The assessment principally arose out of the allegation of respondent's examiner that for the year in question, petitioner admitted having manufactured and sold an average of two (2) units of jeepney per month at an estimated cost of P60,000.00 per unit and that petitioner had an unexplained acquisition of a nine-door apartment in the amount of P400,000.00. Unfortunately, the BIR records failed to show any factual basis to support the findings of the Revenue Examiner that petitioner was producing in 1979 an average of two (2) units of jeepney per month at a cost of P60,000.00 per unit. The examiner's allegation that petitioner had admitted the fact found by him was denied by the petitioner, and even the alleged BLT, Cabuyao Agency list of motor vehicles does not show any sale of jeepney units in 1979 by petitioner. The list only shows a sale made by petitioner of two (2) units in 1992. Such being the case, we are inclined to believe petitioner's allegation that the basis of the assessment was a mere product of the imagination or conjecture of the Revenue Examiner or probably based on mere hearsay or bare assumption and therefore said assessment is clearly contrary to the ruling of the Supreme Court in the case of Collector of Internal Revenue vs. Benipayo, 4 SCRA 182:

> "xxx. An assessment fixes and determines the tax liability of a taxpayer. As soon as it is served, an obligation arises on the part of the taxpayer concerned to pay the amount assessed and demanded. Hence, assessments should not be based on mere presumptions no matter how reasonable or logical said presumptions may be. xxx.
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> "In order to stand the test of judicial scrutiny, the assessment must be based on actual facts. The presumption of correctness of assessment being a mere presumption cannot be made to rest on another presumption xxx."

However, the court finds valid basis in the finding of respondent that petitioner has an "unexplained source of income" for the year in question in the amount of P243,451.19 which must be taxed. Petitioner has justified the purchase price of his apartment in the amount of P400,000.00 only from a cash on hand of P16,548.81 and proceeds of his loan from PNB in the amount of P140,000.00. This is in fact shown in his 1979 income tax return and financial statement. However, as to other loans allegedly procured from other persons to augment his resources to be able to raise the total purchase price of P400,000.00, the same are unsupported by any evidence whatsoever, and therefore, cannot be admitted by this court. The fact that the sale of the said nine door apartment was later on cancelled is of no significance to the resolution of the tax liability of petitioner.

Anent the other issue on whether or not petitioner may be classified as a manufacturer and thus may or may not be qualified as a tax-exempt individual or entity under the NACIDA Law, the same has been rendered moot and academic by our preceding opinion that no factual basis exists to justify that petitioner was a manufacturer of jeepneys in 1979. Furthermore, on the NACIDA tax exemption incentives, it appears from petitioner's income tax return and financial statement that he never actually engaged in said metalcraft industry and, in fact, did not claim a tax exemption privilege in his income tax return. As testified to by petitioner's witness, Mr. Fernando Marceliana, the accountant of petitioner, the metalcraft business income was negligible (p. 24, TSN, August 26, 1992). The bulk of petitioner's income for said year was derived from motor vehicles repair service.

As to the 50% fraud penalty, the aforementioned facts do not necessarily show fraudulent acts on the part of the petitioner that would justify the imposition of said penalty. The fact that this court sustains a portion of the subject BIR assessment does not mean that petitioner is guilty of fraud. Such finding merely results from petitioner's failure to fully substantiate the purchase price of his apartment with sufficient proof or evidence. Fraud is never presumed but must be proven with substantial and positive evidence (Collector vs. Benipayo, *supra*.).

WHEREFORE, the decision appealed from is hereby modified. The assessment for deficiency percentage tax and penalties in the amount of P503,702.00 is hereby nullified, while that covering the income tax liability is recomputed and reduced as follows:

Net income per return			P 18,505.81
Add Unexplained source of income:			
Purchase of commercial building		P400,000.00	
Less: a) cash on hand, 12/31/79	P16,548.81		
b) loans payable -PNB	140,000.00	156,548.81	243,451.19
Net income per Court computation			261,957.00
Less personal exemptions			6,000.00
Net taxable income			P255,957.00
Tax due thereon			P138,731.19
Less tax paid per return			1,292.00
Deficiency income tax			P137,439.19
Add: a) interest on deficiency under Sec. 51(d) maximum of 3 years			
14% [4-16-80 to 7-31-80]		5,640.65	
20% interest [8-1-80 to 4-15-83]		74,405.43	80,046.08
TOTAL AMOUNT DUE AND COLLECTIBLE			P217,485.27*

(*Plus interest and surcharge pursuant to Section 51(e) and (3) of the 1979 Tax Code which shall be computed as the time of payment of subject tax liability.)

SO ORDERED.

ERNESTO D. ACOSTA
Presiding Judge

WE CONCUR:

MANUEL K. GRUBA
Associate Judge

RAMON O. DE VEYRA
Associate Judge

CERTIFICATION

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

ERNESTO D. ACOSTA
Presiding Judge
Court of Tax Appeals