REPUBLIC OF THE PHILIPPINES
Court of Tax Appeals
QUEZON CITY

SPECIAL FIRST DIVISION

SARANGANI RESOURCES CORPORATION,
Petitioner,

versus

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

CTA Case No. 8105

Members:

Uy, *Chairperson, and*
Fabon-Victorino, *JJ.*

Promulgated:
JUN 28 2013, 3:04 p.m.

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DECISION

UY, J.,

This is a Petition for Review filed on May 13, 2010 by petitioner, Sarangani Resources Corporation, to appeal the inaction of respondent, Commissioner of Internal Revenue on its protest letter dated August 28, 2009[1] to the Decision dated July 15, 2009[2] of Atty. Marcelinda Omila-Yap, Regional Director of Revenue Region No. 18, assessing petitioner of deficiency income tax, value-added tax (VAT), and compromise penalty covering calendar year 2005, in the aggregate amount of P1,465,113.20.

THE FACTS

Petitioner Sarangani Resources Corporation is a domestic corporation organized for the purpose of and engaged in the acquisition of real property, subdivision business; ownership, development, construction and operation of resorts, golf courses,

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[1] Exhibit "O", Docket, pp. 998 to 1009.
[2] Exhibit "T", Docket, pp. 1028-1032; Exhibit "17", Docket, pp. 2316-2320.

hotels, beach houses, tennis courts and other structure for tourism purposes on acquired real estate; improvement, development and management of acquired real estate and the construction and alteration on any lands owned, held or occupied buildings and other structures; sale, lease mortgage or disposition of lands or interest therein and in buildings and other structures; production and sale of agricultural products; and the operation of plants, mills, depots, factories and machineries of all kinds for the manufacture of articles of all kinds on the manufacture of which agricultural products are used.[3] Petitioner's office address is located at Cannery Housing, Cannery Site, Polomolok, South Cotabato.

On the other hand, respondent is the duly appointed Commissioner of the Bureau of Internal Revenue (BIR), authorized to review protests on deficiency tax assessment. She holds office at the 5th Floor, BIR National Office Building, Diliman, Quezon City.

In May of 2007, petitioner was furnished a copy of Letter of Authority No. 00057657, authorizing Revenue Officer Adia P. Macasindi supervised by Revenue Officer Evelyn T. Mallillin of Revenue District Office No. 111, Koronadal City to conduct an examination of petitioner's books of accounts and other accounting records for the verification of its tax liabilities for the calendar year ending 31 December 2005.[4]

During the audit period, petitioner submitted to respondent, through Myrna L. Bernardo, OIC-Revenue District Officer of Revenue District Office No. 111, the relevant documents pursuant to the various letter requests of the latter.[5]

On July 15, 2008, petitioner received a Notice for Initial Conference together with a schedule of tax deficiency and the details of discrepancies based upon the investigation conducted by the revenue officer.[6]

On November 12, 2008, petitioner received a copy of the Preliminary Assessment Notice (PAN) issued by Mamapok G. Diro, Assistant Regional Director of Revenue Region No. 18, stating therein that after investigation it was found that petitioner has deficiency

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[3] Par. 1, Admitted Facts, Joint Stipulation of Facts and Issue (JSFI), docket, pp. 144-145.
[4] Par. 3, Admitted Facts, JSFI, docket, p. 145.
[5] Exhibits "B" to "B-2", "F", "G" to "G-3", and "H".
[6] Exhibits "I" to "I-2"; Exhibits "5" and "6".

income and value-added taxes for calendar year 2005 amounting to P3,049,115.31, broken down as follows: P2,831,888.64 as income tax payable and P217,226.67 as value-added tax payable.[7]

On November 26, 2008, Carlos S. Baldostamon, Jr., the President of petitioner submitted two (2) letters both dated November 21, 2008 to Mamapok G. Diro, Assistant Regional Director of respondent, requesting a reconsideration and an extension of time within which to file in writing its explanation and to submit all relevant documents supporting its protest.[8]

On December 8, 2008, petitioner received a letter from Esmeralda M. Tabule, Regional Director of BIR Revenue Region No. 18, denying the request for reconsideration and the request for an extension of time to file its written explanation.[9]

On December 22, 2008[10] petitioner received a Formal Letter of Demand (FLD) and Assessment Notice (FAN), with the Details of Discrepancies all dated December 1, 2008 issued by the Regional Director assessing petitioner with a total collectible amount of P1,402,000.00, corresponding to compromise penalties for calendar year 2005, to wit:[11]

Assessment No.: 111-R-05-04-000079(A)/2008	
Income Tax 2005	
Compromise Penalty for Using Unregistered Receipts	P 1,310,000.00
Compromise Penalty for Failure to Issue Receipts	90,000.00
Compromise Penalty for Failure to make Entries in the Books of Accounts	1,000.00
Compromise Penalty for Failure to Register a Line of Business - Selling of Copra	1,000.00
GRAND TOTAL AMOUNT DUE AND COLLECTIBLE	**P 1,402,000.00**

On December 22, 2008[12], petitioner received another Formal Letter of Demand and Assessment Notice, with Details of Discrepancies all dated December 2, 2008,[13] from respondent, through Esmeralda M. Tabule, assessing petitioner for its tax deficiencies amounting to P1,664,546.43, broken down as follows:

[7] Par. 4, Admitted Facts, JSFI, Docket, pp. 145-146; Exhibit "8".
[8] Exhibits "Q" to "Q-2", "R" to "R-2", and "SS".
[9] Exhibits "S" and "SS".
[10] Exhibit "SS".
[11] Par. 5, Admitted Facts, JSFI, Docket, p. 146; Exhibits "13" and "14".
[12] Exhibit "SS".
[13] Par. 7, Admitted Facts, JSFI, Docket, p. 146; Exhibits "11" and "12".

Assessment No.: 111-R-05-04-000079/2008			
Income Tax 2005			
Taxable Income Per Return			P 1,564,598.00
Add: Discrepancies per Investigation:			
1. Disallowed PEZA Expenses		P 1,137,500.00	
2. Disallowed Taxes and Licenses			
- Unsubstantiated Portion	P 425,669.77		
- Prior Year's Expense	155,020.18	580,689.95	
3. Disallowed Utilities			
- Unsubstantiated Portion	P 189,886.75		
- Prior Year's Expense	2,380.45	192,267.20	
4. Unsubstantiated Supplies and Facilities		11,006.95	
5. Disallowed Miscellaneous Expenses			
- Unsubstantiated Insurance Expense	P 18,155.55		
- Prepaid Insurance Expense	1,418.69		
- Unsubstantiated Anniversary & Other Related Expenses	37,725.51		
- Unsubstantiated Donation & Solicitation	56,100.00		
- Unsubstantiated Newspaper & Magazine Subs.	23,978.00		
- Unsubstantiated Appraisal Expense	67,705.00		
- Unsubstantiated Loan Amortization Expense	10,094.27		
- Appraisal - Not Subjected to Expanded WHT	83,486.00		
- Advertising - Not Subjected to Expanded WHT	2,000.00		
- Personal / Unrelated Expense	1,320.00	301,983.02	
6. Disallowed Outside Services			
- Unsubstantiated Security Services	P 6,426.00		
- Outside Services - Not Subjected to EWT	61,049.54		
- Outside Services - Consultation Fee of Prior Year	94,000.00	161,475.54	
7. Disallowed Salaries, Wages& Allowances			
- Unsubstantiated 13th Month Pay	P 132,810.00		
- Bottom Line Bonus - Prior Year's expense	150,391.51	283,201.51	
8. Unsubstantiated Fuel, Oil and Other Transportation Costs		64,825.10	
9. Unsubstantiated SSS, HDMF and Other Contributions		40,115.00	
10. Disallowed Employees Benefits			
- Unsubstantiated Meal Expense	P 38,344.67		
- Prior Year's Expense	8,378.08		
- Unsubstantiated Medical Benefits	325.00	47,047.75	
11. Disallowed Repairs & Maintenance - Not Subjected to EWT		108,179.20	
12. Overstatement of Depreciation		227,940.27	
13. Rent Receivable Offsetted Against Advances From A Related Company		920,061.31	4,076,292.80
Taxable Income Per Investigation			P 5,640,890.80
Income Tax Due Thereon			P 1,833,289.51
Less: Income Tax Paid per Return			925,354.53
Balance			P 907,934.98
Add: 20% Interest per annum from 04-15-06 to 12-31-08			537,085.91
TOTAL AMOUNT DUE			**P 1,445,020.89**
Assessment No.: L/D# 0205-05/2008 (VAT)			
Value Added Tax 2005			
Taxable Sales/Receipts per Return			P 5,664,672.95

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Add: Discrepancies per Investigation:			
1. Rental Income - Not Subjected to Value Added Tax		P 680,502.05	
2. Interest Income - Not Subjected to Value Added Tax		501,788.00	
3. Miscellaneous Income		142,234.00	1,324,524.05
Taxable Sales/Receipts per Investigation			P 6,989,197.00
Output Tax Due			P 698,919.70
Less: Creditable Input Tax Per Return		P 212,813.71	
Less: Unsubstantiated Input Tax		25,500.05	187,313.66
Deficiency Value Added Tax Due			P 511,606.04
Less: Tax Withheld / Paid Per Return			373,673.66
Balance			P 137,932.38
Add: 20% Interest per annum from 01-23-06 to 12-31-08			81,593.16
TOTAL AMOUNT DUE			**P 219,525.54**
GRAND TOTAL AMOUNT DUE AND COLLECTIBLE			**1,664,546.43**

Petitioner was made liable for a total amount of P3,066,546.43, including the compromise penalties.

On January 21, 2009 petitioner protested the foregoing assessment by filing a letter-protest[14] addressed to respondent, through Esmeralda M. Tabule, Regional Director of BIR Revenue Region No. 18, Cotabato City.

On March 19, 2009, petitioner submitted all the relevant documents in support of its protest.[15]

Petitioner received from Regional Director Atty. Marcelinda Omila-Yap a Decision dated July 15, 2009, partially granting the protest of petitioner, together with the attached Recomputation of Tax Liabilities showing a reduction of tax due to P1,465,113.20, detailed as follows:[16]

Recomputation of Tax Liabilities		
I. Income Tax		
Taxable Income per Investigation		P 5,640,890.80
Less: Adjustments		

[14] Exhibits "L", "M" to "M-15", and "SS".
[15] Exhibits "N" to "N-7" and "SS".
[16] Exhibits "17" and "T".

Taxes & Licenses - Prior Year's Expense	P 155,020.18	
Unrelated Expense	1,320.00	
Employees' Benefits - Prior Year's Expense	8,378.08	
Bottomline Bonus	150,391.51	
Depreciation	227,940.27	
Utilities Expense	2,380.45	
Outside Services and Repairs & Maintenance	148,781.74	694,212.23
Taxable Income After Adjustments		P 4,946,678.57
Income Tax		P 1,607,670.54
Less: Tax Paid per Audit		925,351.53
Deficiency Income Tax		P 682,319.01
Add: Interest (4/16/06 to 8/15/09)		454,874.79
Total Income Tax Payable		**P1,137,193.80**
II. Value-added Tax		
Deficiency Value-added Tax		P 137,932.38
Add: Interest (1/26/06 to 8/15/09)		97,987.02
Total Value-added Tax Payable		**P 235,919.40**
III. Compromise Penalties		
Failure to issue receipts		P 90,000.00
Failure to register a line of business - selling of copra		1,000.00
Failure to make entries in the books of accounts		1,000.00
Total		**P 92,000.00**
Total Amount Payable After Adjustments		**P1,465,113.20**

On August 28, 2009, petitioner filed its letter[17] addressed to respondent Commissioner, requesting reconsideration of the Decision issued by Atty. Marcelinda Omila-Yap, pursuant to Section 3.1.5 of Revenue Regulations No. 12-99, which provides, among others, the procedure in elevating taxpayer's protest to the BIR Commissioner within thirty (30) days from date of receipt of the final decision of the BIR Commissioner's duly authorized representative.

On October 15, 2009, petitioner submitted relevant documents in support of its letter dated August 28, 2009.[18]

Due to the inaction of respondent on the said request for reconsideration, petitioner filed on May 13, 2010 the instant Petition for Review praying that the assessment of deficiency income tax, VAT, and compromise penalties in the aggregate amount of

[17] Exhibits "O" to "O-13" and "SS".
[18] Exhibits "P" to "P-16" and "SS".

P1,465,113.20, covering taxable year 2005, be cancelled and withdrawn.

On July 16, 2010, respondent filed her Answer[19] alleging the following defenses:

"12. Petitioner Sarangani Resources Corporation is liable to pay deficiency income tax, value added tax and penalties for calendar year 2005 in the aggregate amount of One Million Four Hundred Sixty Five Thousand One Hundred Thirteen Pesos and 20/100 (P1,465,113.20) including penalties and interest for the following reasons:

12.1 Audit and investigation disclosed that petitioner's items of deductions from gross income such as PEZA fees, taxes and licenses, utilities, supplies and facilities, insurance expense, anniversary and other related expenses, donation and solicitation, appraisal, loan amortization expense, security services, fuel, oil and transportation costs, SSS, HDMF and other contribution, meal expense and medical benefits were not substantiated with proper documentary evidence like official receipts, hence disallowed pursuant to Section 34(A)(1)(b) of the National Internal Revenue Code (NIRC) of 1997, as amended, which provides:

'**Section 34.** *Deductions from Gross Income.* - Except for taxpayers earning compensation income arising from personal services rendered under an employer-employee relationship where no deductions shall be allowed under this Section other than under subsection (M) hereof, in computing taxable income subject to income tax under Sections 24 (A); 25 (A); 26; 27 (A), (B) and (C); and 28 (A) (1), there shall be allowed the following deductions from gross income;

(A) *Expenses.* -

(1) Ordinary and Necessary Trade, Business or Professional Expenses. –

[19] Docket, pp. 92-101.

(a) In General. - There shall be allowed as deduction from gross income all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on or which are directly attributable to, the development, management, operation and/or conduct of the trade, business or exercise of a profession, including:

(i) A reasonable allowance for salaries, wages, and other forms of compensation for personal services actually rendered, including the grossed-up monetary value of fringe benefit furnished or granted by the employer to the employee: Provided, That the final tax imposed under Section 33 hereof has been paid;

(ii) A reasonable allowance for travel expenses, here and abroad, while away from home in the pursuit of trade, business or profession;

(iii) A reasonable allowance for rentals and/or other payments which are required as a condition for the continued use or possession, for purposes of the trade, business or profession, of property to which the taxpayer has not taken or is not taking title or in which he has no equity other than that of a lessee, user or possessor;

(iv) A reasonable allowance for entertainment, amusement and recreation expenses during the taxable year, that are directly connected to the development, management and operation of the trade, business or profession of the taxpayer, or that are directly related to or in furtherance of the conduct of his or its trade, business or exercise of a profession not to exceed such ceilings as the Secretary of Finance may, by rules and regulations prescribe, upon recommendation of the Commissioner, taking into account the needs as well as the special circumstances, nature and character of the industry, trade, business, or profession of the taxpayer: Provided, That any expense incurred for entertainment, amusement or recreation that is contrary to law, morals public policy or public order shall in no case be allowed as a deduction.

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

12.2 Petitioner's prepaid insurance for the period January 1, 2006 to February 28, 2006 and prior year's consultancy services were disallowed as expenses for calendar year 2005 although paid in 2005. The term 'paid' or 'incurred' means that expenses are deductible in the year they are actually paid out, although not actually incurred, applies to taxpayers who keep books on the actual receipts basis. However, taxpayers using the accrual method, such as the petitioner, expenses are deductible in the year incurred, although not actually paid. Hence, these expenses of petitioner were disallowed because petitioner uses the accrual method of accounting.

12.3 Petitioner's expenses not subjected to withholding tax such as payments to Asian Appraisal Company, Inc. and to Engr. Adelino Fulgueras were disallowed because these expenses were not among the exempted services enumerated in Section 2.57.5 of Revenue Regulations No. 2-98, as amended.

12.4 Petitioner presented arguments through its letter dated January 16, 2009 but it was found to be bereft of factual and legal basis to cancel the assessment. Thus, petitioner is liable for deficiency income tax in the amount of P682,319.01.

12.5 Petitioner is also liable for deficiency value added tax in the amount of P137,932.38.

12.6 Verification disclosed that the rental income amounting to P422,628.00 was subjected to 0% VAT and the amount of P45,000 was VAT exempt. However, the summary of rental income and the VAT returns provided by petitioner were uncertified and petitioner failed to submit sufficient evidence to justify that the amounts were not subject to 10% VAT.

12.7 Pursuant to 2.57(A.2) of Revenue Regulations No. 98 as amended, the interest income of petitioner amounting to P501,788.00 is subject to VAT.

12.8 Section 4.113-4(B) provides that issuance of a VAT invoice or VAT receipt on an exempt transaction by a VAT registered person, but fails to display prominently on the invoice or receipt the words 'VAT Exempt Sale', renders the transaction taxable and the issuer shall pay VAT thereon. Hence, the miscellaneous income of petitioner in the amount of P142,234.00 is subject to VAT.

12.9 It is a well settled rule in taxation that the burden of proof is on the taxpayer to present evidence to show the incorrectness of the assessment. Despite re-investigation, petitioner failed to submit all pertinent papers, records and documents which could evidently prove the incorrectness of the assessment made by respondent.

13. The assessment for calendar year 2005 in the amount of P1,465,113.20 was issued in accordance with law and regulations.

14. Well settled is the rule that tax assessments are entitled to the presumption of correctness and made in good faith. The taxpayer has the duty to prove otherwise. In the absence of proof of any irregularities in the performance of duties, an assessment duly made by a Bureau of Internal Revenue examiner, and approved by his superior officers will not be disturbed. All presumptions are in favor of the correctness of tax assessments *(Sy Po vs. Court of Tax*

> *Appeals, 164 SCRA 524).* Dereliction on the part of petitioner to satisfactorily overcome the presumption of regularity and correctness of the assessment will justify the judicial upholding of said assessment notices."

On November 23, 2010, this Court, upon petitioner's Motion for the Commissioning of an Independent Certified Public Accountant[20], appointed Felix H. Garsuta, Jr. as duly commissioned Independent Certified Public Accountant (CPA).[21]

During trial, petitioner presented the following witnesses: Felix H. Garsuta, Jr., the commissioned Independent CPA[22]; Carlos S. Baldostamon, Jr., the President of petitioner[23]; and Algenib T. Aguirre, accountant of petitioner[24]. On the other hand, respondent presented its lone witness, Adiah P. Macasindil on March 6, 2012.[25] Thereafter, on May 31, 2012, petitioner presented its rebuttal witness Ysa-Ines E. Acac, its Liaison Officer.[26]

On October 12, 2012, this case was submitted for decision, considering petitioner's Memorandum filed on September 24, 2012 and respondent's Memorandum filed on October 10, 2012.

THE ISSUE

The parties jointly stipulated one issue[27] for this Court's consideration:

> "1. Whether or not petitioner is liable for the deficiency value added tax, income tax and compromise penalties assessments in the aggregate amount of one million four hundred sixty five thousand one hundred thirteen pesos and twenty centavos (Php1,465,113.20), inclusive of interest and penalty for the taxable year 2005."

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[20] Docket, pp. 186-189.
[21] Minutes of Hearing,Docket, p. 193.
[22] Minutes of Hearing dated February 3, 2011 and March 8, 2011, Docket, pp. 251 and 368.
[23] Minutes of Hearing dated March 8, 2011 and March 31, 2011, Docket, pp. 368, 374-375.
[24] Minutes of Hearing dated May 10, 2011 and June 21, 2011, Docket, pp. 926 and 935.
[25] Docket, p. 2259.
[26] Docket, pp. 2342.
[27] Docket, p. 147.

THE COURT'S RULING

I. INCOME TAX

From the Formal Letter of Demand and Recomputation of Tax Liabilities, the deficiency income tax assessment arose from the following items:

PEZA Expenses - unsubstantiated	P 1,137,500.00
Taxes and Licenses - unsubstantiated	425,669.77
Utilities - unsubstantiated	189,886.75
Supplies & Facilities – unsubstantiated	11,006.95
Insurance Expenses - unsubstantiated	18,155.55
Prepaid Insurance Expense	1,418.69
Anniversary and Other Related Expenses - unsubstantiated	37,725.51
Donation & Solicitation – unsubstantiated	56,100.00
Newspaper and Magazine Subscriptions - unsubstantiated	23,978.00
Appraisal Expense- unsubstantiated	67,705.00
Loan Amortization – unsubstantiated	10,094.27
Appraisal - not subjected to EWT	83,486.00
Advertising - not subjected to EWT	2,000.00
Security Services – unsubstantiated	6,426.00
Outside Services - not subjected to EWT	61,049.54
Outside Services - Consultation Fee of Prior Year	94,000.00
Salaries & Wages - 13th month pay - unsubstantiated	132,810.00
Fuel, Oil & Other Transportation Costs - unsubstantiated	64,825.10
SSS, HDMF & Other Contributions - unsubstantiated	40,115.00
Meal Expenses – unsubstantiated	38,344.67
Medical Benefits – unsubstantiated	325.00
Repairs and Maintenance - not subjected to EWT	108,179.20
Rent Receivable Offsetted Against Advances From a Related Company	920,061.31
Less: Outside Services and Repairs & Maintenance	(148,781.74)
Total	**P 3,382,080.57**

The disallowances from the foregoing table can be summarized as follows:

1. *Unsubstantiated expenses*		
PEZA Expenses - unsubstantiated	P 1,137,500.00	
Taxes and Licenses - unsubstantiated	425,669.77	
Utilities - unsubstantiated	189,886.75	
Supplies & Facilities – unsubstantiated	11,006.95	
Insurance Expenses - unsubstantiated	18,155.55	
Anniversary and Other Related Expenses - unsubstantiated	37,725.51	
Donation & Solicitation - unsubstantiated	56,100.00	
Newspaper and Magazine Subscriptions - unsubstantiated	23,978.00	
Appraisal Expense- unsubstantiated	67,705.00	
Loan Amortization - unsubstantiated	10,094.27	
Security Services - unsubstantiated	6,426.00	

Salaries & Wages - 13th month pay - unsubstantiated	132,810.00	
Fuel, Oil & Other Transportation Costs - unsubstantiated	64,825.10	
SSS, HDMF & Other Contributions - unsubstantiated	40,115.00	
Meal Expenses – unsubstantiated	38,344.67	
Medical Benefits - unsubstantiated	325.00	
Subtotal		P 2,260,667.57
2. *Prepaid Insurance Expense*		1,418.69
3. *Not subjected to EWT*		
Appraisal - not subjected to EWT	P 83,486.00	
Advertising - not subjected to EWT	2,000.00	
Outside Services - not subjected to EWT	61,049.54	
Repairs and Maintenance - not subjected to EWT	108,179.20	
Less: Outside Services and Repairs & Maintenance	(148,781.74)	
Subtotal		105,933.00
4. *Outside Services - Consultation Fee of Prior Year*		94,000.00
5. *Rent Receivable Offsetted Against Advances From A Related Co.*		920,061.31
Total		**P 3,382,080.57**

1. Unsubstantiated expenses – P2,260,667.57

Based on the FLD, respondent's investigation disclosed that there were items of deduction from gross income in the aggregate amount of P2,260,667.57 that were not substantiated with proper documentary evidence such as official receipts; hence, must be disallowed pursuant to Section 34(A)(1)(b) of the NIRC, as amended, broken down as follows:

1.	PEZA Expenses	P 1,137,500.00
2.	Taxes and Licenses	425,669.77
3.	Utilities Expense	189,886.75
4.	Supplies and Facilities	11,006.95
5.	Insurance Expenses	18,155.55
6.	Anniversary and Other Related Expenses	37,725.51
7.	Donation & Solicitation	56,100.00
8.	Newspaper and Magazine Subscriptions	23,978.00
9.	Appraisal Expense	67,705.00
10.	Loan Amortization	10,094.27
11.	Security Services	6,426.00
12.	Salaries & Wages – 13^{th} month pay	132,810.00
13.	Fuel, Oil & Other Transportation Costs	64,825.10
14.	SSS, HDMF & Other Contributions	40,115.00
15.	Meal Expenses	38,344.67
16.	Medical Benefits	325.00
	TOTAL	**P 2,260,667.57**

Petitioner alleges that all of the foregoing expenses, which it claimed as deductions from gross income, were duly substantiated with official receipts.

To refute respondent's findings, the Independent CPA, Felix H. Garsuta Jr., validated and presented a summary[28] together with the supporting documents[29] to prove that all the disallowed expenses as claimed by petitioner are duly supported, as follows:

Exhibit	Account	Total	Validated with supporting documents	Supporting documents with exceptions
V	PEZA Fees	P1,137,500.00	P 1,029,166.73	P 108,333.34
W	Taxes and Licenses	425,669.75	405,322.34	20,347.41
X	Utilities	189,886.75	189,773.55	113.20
Y	Supplies & Facilities	11,006.95	3,425.30	7,581.85
Z	Insurance Expenses	18,155.55	18,155.55	-
AA	Anniversary and Other Related Expenses	37,725.51	31,825.51	5,900.00
BB	Donation & Solicitation	56,100.00	28,000.00	28,100.00
CC	Appraisal	67,705.00	-	67,705.00
DD	Loan Amortization	10,094.27	10,094.27	-
EE	Security Services	6,426.00	6,426.00	-
FF	Fuel, Oil & Other Transportation Costs	64,825.10	299.10	64,526.00
GG	SSS, HDMF & Other Contributions	40,115.00	35,940.00	4,175.00
HH	Meal Expenses	38,344.67	34,198.85	4,145.82
II	Disallowed Miscellaneous Expenses	109,464.00	83,486.00	25,978.00
JJ	Disallowed Salaries & Wages	132,810.00	132,810.00	-
KK	Disallowed Outside Services	169,228.74	142,377.74	26,851.00
	Grand Total	**P2,515,057.29**	**P 2,151,300.94**	**P 363,756.62**

Examination of the Independent CPA's summary shows that medical benefits disallowed in the amount of P325.00 was not included; thus, respondent's assessment on the same shall remain.

Included in the validation of the disallowed Miscellaneous Expenses of P109,464.00 were appraisal and advertising expenses not subjected to EWT in the amounts of P83,486.00 and P2,000.00, respectively; while, the remaining amount of P23,978.00 accounts for the unsubstantiated newspaper and magazine subscriptions.

Disallowed Outside Service in the amount of P169,228.74 pertains to Outside Services and Repairs and Maintenance assessment not subjected to EWT in the amounts of P61,049.54 and P108,179.20, respectively.

Therefore, out of the P2,515,057.29 ascertained by the Independent CPA, only P2,260,342.55 relates to the unsubstantiated

[28] Table 2, Exhibit "QQ", Docket, p. 1547.
[29] Exhibits "V" to "V-18", "W" to "W-7", "X" to "X-23", "Y" to "Y-9", "Z" to "Z-2", "AA" to "AA-9", "BB" to "BB-12", "CC" to "CC-4", "DD" to "DD-1", "EE" to "EE-1", "FF" to "FF-15", "GG" to "GG-14", "HH" to "HH-20", "II" to "II-22", "II-24" to "II-28"," JJ" to" JJ-4", and "KK" to "KK-36".

disallowances and only the amount of P1,925,437.20 was validated with supporting documents by the Independent CPA, as follows:

Account	Total	Validated with supporting documents	Supporting documents with exceptions
Ascertained by ICPA per Summary	P 2,515,057.29	P 2,151,300.94	P 363,756.62
Less: Assessments - not subjected to EWT			
Appraisal Costs - included in Exhibit "II"	(83,486.00)	(83,486.00)	-
Advertising Expense - included in Exhibit "II"	(2,000.00)	-	(2,000.00)
Outside Services - Exhibit "KK"	(61,049.54)	(142,377.74)	(26,851.00)
Repairs and Maintenance Expense - Exhibit "KK"	(108,179.20)		
Ascertained by the ICPA re unsubstantiated portion	**P 2,260,342.55**	**P 1,925,437.20**	**P 334,905.62**

However, a scrutiny of the supporting documents[30] submitted reveal that out of the P1,925,437.20 validated with supporting documents by the Independent CPA, only the amount of P1,376,292.05 was properly supported, while the amount of P549,145.15 should still be disallowed for the reasons stated below, to wit:

1. OR/invoice not payable to Sarangani Resources Corp.			
TAXES AND LICENSES			
Exhibit	**OR No.**	**Amount**	**Remarks**
W-3	6404015	P 20,547.80	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37467	31,424.03	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37468	2,188.26	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37469	34,436.22	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37470	19,469.74	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37471	389.87	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37472	11,842.88	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37473	27,346.50	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37474	13,432.27	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37475	27,648.91	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37476	2,493.64	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37477	837.76	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37478	9,195.13	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37479	8,793.50	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37480	17,048.09	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37481	993.50	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37482	990.67	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37483	131.35	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37484	437.48	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37485	295.58	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37486	143.99	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37487	130.30	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37488	1,160.70	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37489	4,783.06	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37490	4,957.84	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)

[30] Exhibits "V" to "V-18", "W" to "W-7", "X" to "X-23", "Y" to "Y-9", "Z" to "Z-2", "AA" to "AA-9", "BB" to "BB-12", "CC" to "CC-4", "DD" to "DD-1", "EE" to "EE-1", "FF" to "FF-15", "GG" to "GG-14", "HH" to "HH-20", "II" to "II-22", "II-24" to "II-28"," JJ" to" JJ-4", and "KK" to "KK-36".

W-4	37491	4,957.84	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37492	3,730.65	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37493	3,796.10	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-4	37494	26,841.79	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-6	9233225	354.24	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-6	9233226	71.36	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-6	9233227	810.00	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
W-6	9233228	15,185.84	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
Subtotal		**P 296,866.89**	
UTILITIES			
Exhibit	**OR No.**	**Amount**	**Remarks**
X-1	75003-04	P 2,380.45	OR payable to SRC Office
X-2	7881830	370.41	OR payable to L-2 Apt.
X-4	81476	778.25	OR payable to SRC Office
X-6	7970131	240.56	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
X-6	7970133	338.03	OR payable to L-2 Apt.
X-7	86412-13	539.55	OR payable to SRC Office
X-8	8094997	2,514.45	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
X-9	8094995	297.36	OR payable to L-2 Apt.
X-10	8107789	3,228.16	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
X-11	8107790	297.28	OR payable to L-2 Apt.
X-12	8164234	3,131.27	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
X-12	8164236	411.19	OR payable to L-2 Apt.
X-13	102982-83	528.15	OR payable to SRC Office
X-14	108493-94	512.75	OR payable to SRC / SRC Office
X-15	8217018	414.88	OR payable to L-2 Apt.
X-15	8217020	2,959.99	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
X-17	8542782	2,941.77	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
X-17	8542783	354.21	OR payable to L-2 Apt.
X-19	8545129	3,837.16	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
X-20	8563831	3,350.42	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
X-20	8563832	577.67	OR payable to L-2 Apt.
X-21	8734811	3,805.47	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
X-21	8734812	979.12	OR payable to L-2 Apt.
X-23	113751-52	585.30	OR payable to SRC / SRC Office
X-22	8219391	2,663.11	OR payable to Sarangani Realty Corp (allegedly petitioner's old name)
Subtotal		**P 38,036.96**	
SUPPLIES AND FACILITIES			
Exhibit	**Invoice No.**	**Amount**	**Remarks**
Y-2		P 677.50	OR with no payor and blurred (not legible)
Y-2	3699	267.95	Cash invoice payable to SRC
Y-4	24126	950.00	Cash invoice payable to SRC
Y-6	55032	1,529.85	OR payable to SRC
Subtotal		**P 3,425.30**	
ANNIVERSARY AND OTHER RELATED EXPENSES			
Exhibit	**OR No.**	**Amount**	**Remarks**
AA-3	8468882	P 337.81	OR payable to L-2 Apt.
AA-4	12274	8,246.00	OR payable to SRC (supporting invoice payable to Sarangani Realty Corp & Mahintana Foundation Inc.)
AA-5	19475	964.00	Cash invoice payable to SRC
AA-6	15959-60	602.70	OR payable to SRC / SRC Office
AA-8	1035-A	75.00	OR payable to Acac, Ysa
AA-9	1832	21,600.00	OR payable to SRC
Subtotal		**P 31,825.51**	

DONATION & SOLICITATION			
Exhibit	**OR No.**	**Amount**	**Remarks**
BB-3	164	P 4,000.00	OR payable to SRC / Sarangani Realty Corp.
BB-9		2,000.00	OR payable to SRC
Subtotal		**P 6,000.00**	
FUEL, OIL AND OTHER TRANSPORTATION COSTS			
Exhibit	**Invoice No.**	**Amount**	**Remarks**
FF-5	20595	P 299.10	OR payable to SRC
Subtotal		**P 299.10**	
MEAL EXPENSES			
HH-1	3355	P 1,409.00	OR payable to Carlos S. Baldostamon / SRC
HH-3	11943	1,010.00	OR payable to SRC & Invoice payable to SRC/Sarangani Realty Corp.
HH-4	18732	630.70	Cash invoice payable to SRC
HH-5	various	1,938.82	OR payable to SRC
HH-6	11595	14,133.00	OR payable to SRC and charged invoice to Mahintana
HH-7	9476	762.14	Cash invoice payable to SRC
HH-8	9054	1,790.34	Cash invoice payable to SRC
HH-9	various	1,354.58	OR / Invoice payable to SRC
HH-10	2455	1,228.00	OR payable to SRC
HH-11	1115	290.91	Cash invoice payable to SRC
HH-12	various	890.00	Cash invoice payable to SRC / C
HH-13	12287	4,141.00	OR payable to SRC
HH-14	various	928.18	Cash invoice payable to SRC
Subtotal		**P 30,506.67**	
Total		**P 406,960.43**	
2. Not yet a valid expense of taxable year 2005 (Pre-payments).			
INSURANCE EXPENSES			
Exhibit	**OR No.**	**Amount**	**Remarks**
Z-2	193353	P 7,374.72	for January 1 to September 2, 2006 (₱11,062.08 x 8/12)
Total		**P 7,374.72**	
3. Supported by bank deposit slip and voucher only.			
DONATION & SOLICITATION			
Exhibit	**OR No.**	**Amount**	**Remarks**
BB-6		P 2,000.00	supported by bank deposit slip in the account name of Roger Corea
Total		**P 2,000.00**	
4. Supported by self-serving check vouchers and payroll slip only.			
DISALLOWED SALARIES AND WAGES			
JJ	total	P 132,810.00	supported by self-serving check vouchers and payroll slips only
Total		**P 132,810.00**	
Grand Total		**P 549,145.15**	

2. Prepaid Insurance Expense – P1,418.69

Respondent disallowed the amount of P1,418.69 for Prepaid Insurance Expense, recorded by petitioner as Miscellaneous Expense, as deduction from gross income pursuant to Section 34(A)(1)(a) of the NIRC of 1997.

Petitioner explained that the Prepaid Insurance Expense of P1,418.69 (P8,512.16 x 2 ÷ 12) pertains to the unamortized portion for January 1, 2006 to February 28, 2006 of the Prepaid Vehicle Insurance for a Mitsubishi L-200 Double Cab Pick-Up Timber Green covering the period of March 1, 2005 to February 28, 2006. Such prepaid insurance expense was paid per Check Voucher No. 2961 dated February 21, 2005 under Official Receipt No. 01071492. The total premium for the said insurance policy is P8,512.16, whereby P7,093.47 corresponds to insured months within calendar year 2005 and the remaining balance of P1,418.69 represents the premium allocated for January 1, 2006 to February 28, 2006. Further, the prepaid insurance expense of P1,418.69 was an ordinary and necessary expense paid during calendar year 2005, and hence, it was a valid deduction from gross income pursuant to Section 34(A)(1)(a) of the NIRC of 1997, as amended.[31]

Moreover, petitioner argues that regardless of the fact that certain portions of the total insurance premium are allotted for months beyond the 2005 calendar year, the total prepaid expense shall be considered as having accrued within calendar year 2005 given that upon availing the prepaid insurance, the liability for the satisfaction of the total premium became due and the amounts for each month of the covered period are determinable by simple computation. The expense, being fixed and determinable in amount in calendar year 2005, is deemed to have accrued then.[32]

Under Section 34 of the NIRC of 1997, as amended, allowing the deductions of all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, three (3) necessary conditions are imposed for the deductibility of business expenses, namely: (1) the expense must be ordinary and necessary; (2) it must be paid or incurred within the taxable year; and (3) it must be paid or incurred in carrying on a trade or business.[33] "Paid" or "incurred" means that expenses are deductible in the year that they are actually paid out by the taxpayer who keeps his books on the actual receipts basis and deductible in the year incurred, although not actually paid by a taxpayer who keeps his books on the accrual basis.[34]

[31] No. 5 of Letter B, Exhibit "16", Docket, pp. 2308-2309; Nos. 64-65, Memorandum, Docket, p. 2787.

[32] Nos. 66 and 67, Memorandum, Docket, p. 2787.

[33] *Moneyline Telerate (Philippines), Inc. vs.* Commissioner of Internal Revenue, CTA Case No. 7658, February 4, 2011, citing *Collector of Internal Revenue vs. Philippine Education Co.,* 99 Phil. 319, May 30, 1956.

[34] *Moneyline Telerate (Philippines), Inc. vs.* Commissioner of Internal Revenue, CTA Case No. 7658, February 4, 2011, citing *Paper Industries Corporation of the Philippines vs. Commissioner of Internal Revenue,* CTA Case No. 3458, January 29, 1988.

Petitioner does not dispute that its records are kept on the accrual basis. It is to be noted that accrual method of accounting recognizes the expenses in the period they are incurred and not in the period they are paid. Since the portion of insurance payment in the amount of P1,418.69 has not yet been incurred, although already paid, as the same is allocated as expense for January and February of the following taxable year, the same shall not be considered as allowable deduction from its income for taxable year 2005.

3. Not subjected to 2% Expanded Withholding Tax – P105,933.00

Section 34(K) of the NIRC of 1997, as amended, provides:

> "SEC. 34. *Deductions from Gross Income.* - xxx
>
> (K) *Additional Requirements for Deductibility of Certain Payments.* - Any amount paid or payable which is otherwise deductible from, or taken into account in computing gross income or for which depreciation or amortization may be allowed under this Section, shall be allowed as a deduction only if it is shown that the tax required to be deducted and withheld therefrom has been paid to the Bureau of Internal Revenue in accordance with this Section, Sections 58 and 81 of this Code."

Pursuant to the foregoing provision, in computing gross income, only income payments that were subjected to the expanded withholding tax shall be allowed as deductible expenses. Respondent disallowed petitioner's expenses in the total amount of P105,933.00, pursuant to Section 34(K) of the NIRC in relation to Section 2.57.2 of Revenue Regulations (RR) No. 2-98, as amended, due to petitioner's alleged failure to subject several expenses to expanded withholding tax. The disallowed expenses which were not subjected to 2% EWT are as follows:

Appraisal Costs		P 83,486.00
Advertising Expense		2,000.00
Outside Services	P 61,049.54	
Repairs and Maintenance Expense	108,179.20	

Less: Outside Services and Repairs and Maintenance	(148,781.74)[35]	20,447.00
Total		**P105,933.00**

a. Appraisal Costs – P83,486.00

Petitioner claims that it did not withhold any tax at source for the appraisal and preparation of subdivision survey of petitioner's properties by Asian Appraisal Co., Inc. and Adelino Fulgueras, respectively, because unlike the service contracts with security agencies which are valid for twelve months and renewable every year, these were one-time service contracts for inventory purposes only.[36]

Considering that the said services are not one of those enumerated as exempted from EWT under Section 2.57.5 (Exemption from Withholding) of Revenue Regulations No. 2-98, as amended, respondent's disallowance corresponding to these income payments shall be sustained.

b. Advertising Expense – P2,000.00

Petitioner claims that advertising expense pertains to the payment made to Mt. Matutum, the Newsmaker for a ¼ page advertisement in their special issue. Petitioner did not subject this expense to expanded withholding tax because it was incurred in support of the 48th Foundation Anniversary celebration of Polomolok and 2nd F'lomlok Festival on September 6-10, 2005.[37]

However, petitioner failed to adduce any documentary evidence to support its claim. Therefore, the disallowance of advertising expense amounting to P2,000.00 shall remain.

c. Outside Services and Repairs & Maintenance – P20,447.00 (net)

Respondent discovered that P61,049.54 Outside Services Costs and P108,179.20 Repairs and Maintenance Expense (Services) paid to contractor (or a total amount of P169,228.74) were not subjected to 2% EWT. Out of the aggregate amount of P169,228.74, petitioner

[35] Exhibit "17", Docket, pp. 2316-2320.
[36] No. 6 of Letter B, Exhibit "16", Docket, p. 2309.
[37] No. 7 of Letter B, Exhibit "16", Docket, p. 2310.

allegedly contracted P148,781.74 worth of services from three (3) multi-purpose cooperatives with Certificates of Tax Exemption from the BIR, namely: (1) FARB Multi-purpose Cooperative; (2) PSW Multi-purpose Cooperative; and (3) UEMS Multi-purpose Cooperative. As such, payments to these cooperatives for taxable year 2005 were not subjected to the 2% EWT. In a letter dated July 15, 2009,[38] the BIR already considered the said payments to cooperatives exempt from withholding. As to the remaining expenses assessed by the BIR in the amount of P20,447.00, the same shall be sustained because petitioner did not present supporting documents to prove that those are indeed not to be subjected to EWT.

4. Outside Services – Consultation Fee of Prior Year – P94,000.00

Respondent's investigation disclosed that Consultancy Fees of P94,000.00 recorded in Outside Services account were payments to services incurred in the prior years, hence, disallowed pursuant to Section 34(A)(1)(a) of the NIRC.

Petitioner avers that this deduction pertains to payment of consultancy fee and transportation allowance to Ben L. Perez for January and February 2005. To the mind of the Court, this Outside Services expense consisting of consultancy fee and transportation allowance in the aggregate amount of P94,000.00 was an ordinary and necessary expense, paid or incurred during taxable year 2005. Thus, it is a valid deduction from gross income pursuant to Section 34(A)(1)(a) of the NIRC of 1997, as amended.

However, aside from check vouchers[39], petitioner failed to present relevant documents to support its allegations, such as but not limited to billing/sales invoices and official receipts issued by Mr. Ben L. Perez. Thus, the P94,000.00 disallowance of Consultancy Fee of prior year shall remain.

5. Rent Receivable Offsetted Against Advances – P920,061.31

Respondent's examiner found that this item of deduction amounting to P920,061.31 was claimed as payments to a related

[38] Exhibit "17", item c, Docket, p. 2316.
[39] Exhibit "LL", Docket, p. 1517.

company as presented in the Statement of Cash Flows. However, the supporting documents submitted before the BIR during the investigation supposedly disclosed that this was originally taken up as part of the company's receivable which was then directly offsetted against the Advances from a stockholder and a related company. It was found that no actual cash payment was made, hence, should be added back to the cash account and should form part of the taxable income.

Petitioner claims that as an audit adjusting entry for calendar year 2005, the land rentals of DOLEFIL, a related company, for period 13 of calendar year 2005 were credited to Industrial Land Rental and (VAT) Output Tax to accrue the income for the month of December and debited to Due to Affiliate account in the same amount in order to reduce its liability with DOLEFIL as of December 31, 2005. As such, the subject amount was already declared as income for calendar year 2005. Meanwhile, the (VAT) Output tax relative to this transaction was remitted on February 7, 2006, together with the Output Tax for January 2006. However, upon receipt of DOLEFIL's payment in January 2006, the said amount credited by the bank to petitioner's account was mistakenly taken up in the General Journal through JV#s 2006-001 up to 004 as rental income for 2006. At any rate, the said Journal Voucher entries were reversed on June 30, 2006 to correct the overstatement in the 2006 rentals. Accordingly, the amount of P920,061.31 paid to DOLEFIL was properly claimed as deduction from gross income.[40]

Petitioner argues that there is no need to add back the amount of P920,061.31 to the income when it has already been taken up as rental income before it was offset against Advances to Affiliates. Moreover, said amount was allegedly also taken up as various expenses in previous entries made to accrue petitioner's liability to its affiliate from January 2005 up to December 2005.[41]

Purportedly, the Independent CPA was able to trace the journal entries corresponding to the rental transactions. The Independent CPA also claims that it has traced OR No. 1118 representing land rental receipts for period 13 2005 and the related Journal Voucher to take up the reversal entry due to double take up.[42] However, the Summary of general journal, bank passbook entry and official

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[40] No. 14, Exhibit "16", Docket, p. 2313
[41] Exhibit "O-5", Docket, pp. 1003-1004.
[42] C.2, Exhibit "QQ", Docket, p. 1564.

receipt[43] submitted are not enough to dispute the same. The disallowance is proper considering that petitioner failed to establish the direct relation of the rent receivable which was offsett against advances.

In sum, petitioner's basic deficiency income tax amounts to **P235,021.09**, computed as follows:

Taxable Income per respondent's recomputation	P 4,946,678.57
Less: Substantiated Disallowances	1,376,292.05
Taxable Income After Adjustments	P 3,570,386.52
Income Tax Due Thereon	P 1,160,375.62
Less: Tax Paid per Return	925,354.53
Basic Deficiency Income Tax	**P 235,021.09**

II. VALUE-ADDED TAX

Respondent assessed petitioner for deficiency value-added tax for the year 2005, to wit:[44]

Taxable Sales/Receipts per Return		P 5,664,672.95
Discrepancies per investigation:		
1. Rental income - not subjected to VAT	P 680,502.05	
2. Interest income - not subjected to VAT	501,788.00	
3. Miscellaneous income	142,234.00	1,324,524.05
Vatable sales/Receipts per return per investigation		P 6,989,197.00
Output tax due		P 698,919.70
Less: Creditable tax per return	P 212,813.71	
Less: Unsubstantiated input tax	25,500.05	187,313.66
Deficiency VAT due		P 511,606.04
Less: Tax withheld per return		373,673.66
Balance		P 137,932.38
Add: 20% Interest p.a. (1.26.06 to 8.15.09)		97,987.02
Total amount due		**P 235,919.40**[45]

Petitioner filed its protest to the Formal Letter of Demand on January 21, 2009[46] and submitted the supporting documents on March 19, 2009.[47] Thereafter, BIR Regional Director Atty. Marcelinda Omila-Yap responded to petitioner's protest and stated in her Decision dated July 15, 2009, thus:[48]

[43] Exhibits "NN" to "NN-1".
[44] Exhibits "11" and "12".
[45] Recomputed as per Annex "A", Exhibit "T", docket, p. 1032; Exhibit "17", Docket, p. 2320.
[46] Exhibits "M" to "M-15", Docket, pp. 978-991.
[47] Exhibits "N" to "N-7", Docket, pp. 992-997.
[48] Exhibits "T" to "T-3", Docket, pp. 1028-1031.

"However, as regards the assessment on the following items, the same stands in view of the following, viz:

xxx xxx xxx

C. Value-added Tax

1. Verification of rental income revealed discrepancy on the amount subjected with 10% VAT amounting to P467,628.00. The submitted Summary of Rental Income showed that P422,628.00 was subjected with 0% VAT and P45,000.00 was VAT-exempt. However, the Summary of Rental Income and VAT Returns were uncertified and there was no sufficient evidence was found to justify that such discrepancy should not be subjected to 10% VAT.

2. It was contended that the interest income amounting to P501,788.00 earned from savings deposit should not be subjected to VAT for the reason that it was already subjected with final withholding tax. However, Section 2.57(A.2) of Revenue Regulations No. 2-98, as amended, states that, 'The finality of the withholding tax is limited to the payee's income tax liability on the particular income. It does not extend to the payee's other tax liability on the said income, such as when the said income is further subject to a percentage tax.' Thus, the assessment stands.

3. The **Sec. 4.113-4(B) – Consequences of Issuing Erroneous VAT Invoice or VAT Official Receipt** provides that, '(B) Issuance of a VAT Invoice or VAT Receipt on an Exempt Transaction by a VAT-registered Person – If a VAT-registered person issues a VAT invoice or VAT official receipt for a VAT-exempt transaction, but fails to display prominently on the invoice or receipt the words 'VAT-exempt sale', the transaction shall become taxable and the issuer shall be to pay VAT thereon. The purchaser shall be entitled to claim an input tax credit on his purchase.' Hence, the VAT assessment on the P142,234.00 Miscellaneous Income still stands.

4. No documents were submitted to refute the P25,500.00 input tax disallowance."

The Court shall discuss each item in the subject deficiency VAT assessment.

1. Rental Income Not Subjected to VAT - P680,502.05

Scrutiny of the Summary of Rental Income for 2005 revealed the following:[49]

Client/ Customer	Total Rental Income	Subject to 10% VAT	Subject to 0% VAT	VAT Exempt	VAT (Output)
Dole Philippines	P 9,623,590.00	P 5,850,273.00	P3,773,316.00	P -	P 585,027.00
SMI	27,274.00	27,274.00			2,726.00
Dept. of Agrarian Reform	30,000.00		30,000.00		-
Mahintana Foundation Inc.	45,000.00			45,000.00	-
TOTAL	**P9,725,863.00**	**P5,877,547.00**	**P3,803,316.00**	**P45,000.00**	**P587,754.00**

The total rental income of P9,725,863.00 corresponds to petitioner's rental income reported in its Audited Financial Statements[50] and declared revenue/receipts in its Annual Income Tax Return for the year 2005.[51] Respondent's examiner found that of this amount, the amount of P3,380,688.00 was generated from its properties within the ecozone, which is subject to zero percent (0%) VAT. The remaining P6,345,175.00 should be subjected to VAT, but per VAT Returns, only P5,664,672.95 was subjected to VAT.[52] As a result, in the Formal Letter of Demand, petitioner was assessed for deficiency VAT for the discrepancy on rental income of P680,502.05, computed as follows:

Rental income that should be subject to VAT	P6,345,175.00
Rental income per VAT Returns[53]	*5,664,672.95
Difference	**P680,502.05**

** Note that the taxes due per "UU-21" to "UU-34" were divided by 10% tax rate to arrive at the gross rental income, as computed below:*

Covered Period (CY 2005)	10% VAT	Gross Rental Income
1st Quarter	P 232,529.31	P 2,325,293.22

[49] Exhibit "UU", docket, p. 2169.
[50] BIR Records, pp. 17 to 27.
[51] BIR Records, pp. 16 and 28.
[52] Revenue Officer's Narrative Report/Memorandum dated September 1, 2008, BIR Records, pp. 160 to 164.
[53] Exhibits "UU-9", "UU-18", and "UU-21" to "UU-34".

2nd Quarter	192,562.83	1,925,628.33
July	23,257.67	
August	23,257.67	
September	23,257.67	
October	23,257.67	
November	46,515.34	
December	1,829.12	
Total - July to December	P 141,375.14	
Divided by 10% VAT Rate	10%	1,413,751.40
Sales/Receipts subject to 10% VAT per Return		**P 5,664,672.95**

Of the discrepancy of P680,502.05, the amount of P45,000.00 was allegedly exempt from VAT and P422,628.00 was subjected to 0% VAT, computed thus:

	Rental income subject to 0% VAT
Per Summary of Rental Income for 2005	P 3,803,316.00
Per respondent's examiner's findings	3,380,688.00
Difference	**P 422,628.00**

As to the remaining amount of P212,874.05 being subjected by respondent to 10% VAT, petitioner did not present any evidence to refute the findings of respondent. Consequently, respondent's assessment thereon shall remain.

As regards respondent's findings of P45,000.00 as rental income exempted from VAT, the same pertains to petitioner's rental income from Mahintana Foundation Inc. However, petitioner failed to submit documents to show that the transaction with said client/customer is VAT-exempt.

Petitioner claims that pursuant to the Certification on the entitlement to VAT zero-rating issued by PEZA to Dole Philippines, Inc. (DPI), there is legal basis not to subject the rental income due from the former, pertaining to the lease of industrial land, specifically, the Calumpang Cannery Plant and the Polomolok Cannery Plant to 10% VAT.[54] Petitioner submitted the PEZA Certification of DPI[55] to support the zero-rating of its rental income from DPI. However, the Court observes from the Summary of Rental Income for 2005 that petitioner's rental income from said PEZA-registered entity consisted of income subject to 10% VAT, as well as

[54] Exhibit "O-9", Docket, p. 1007.
[55] Exhibits "PP" and "PP-1", Docket, pp. 1531-1534.

to 0% VAT. Without other supporting documents, such as petitioner's detailed books of accounts pertaining to rental income from DPI, the Court could not ascertain whether or not the amount of rental income subjected to 0% VAT is correct.

Hence, for failure to satisfactorily controvert the findings of respondent's examiner, the deficiency VAT assessment on rental income amounting to P680,502.05 shall be upheld.

2. Interest Income Not Subjected to VAT - P501,788.00

Respondent's examiner found interest income in the amount of P501,788.00 from petitioner's savings deposit account[56] and assessed the same for deficiency VAT pursuant to Section 2.57(A) of Revenue Regulations No. 2-98, as amended.[57]

Petitioner argues that the said interest income was earned from its savings account in RCBC which was credited directly to petitioner's account at the end of every quarter and also from its Certificates of Time Deposit (monthly/upon maturity) for calendar year 2005. Considering that said interest income is net of the 20% Final Tax already withheld by the bank upon payment or credit, petitioner must no longer be subjected to VAT on interest income.[58]

Section 2.57(A) of Revenue Regulations No. 2-98 provides:

> "SECTION 2.57. *Withholding of Tax at Source.* -
>
> (A) *Final Withholding Tax.* - xxx
>
> The finality of the withholding tax is limited only to the payee's income tax liability on the particular income. It does not extend to the payee's other tax liability on said income, such as when the said income is further subject to percentage tax. For example, if a bank receives income subject to final withholding tax, the same shall be subject to a percentage tax."

While the above-quoted provision is true, the assessment of

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[56] Exhibits "MM" to "NN-1", Docket, pp. 1518-1527.
[57] Exhibit "12", Docket, p. 2298.
[58] Exhibit "16", Docket, p. 2314.

deficiency VAT on petitioner's interest income is misplaced. Sections 4.105-1 and 4.105-2 of Revenue Regulations No. 16-2005, the Consolidated Value-Added Tax Regulations of 2005, are quoted hereunder for easy reference:

> "SECTION 4.105-1. *Persons Liable.* - **Any person who, in the course of his trade or business, sells, barters, exchanges or leases goods or properties, or renders services, and any person who imports goods**, shall be liable to VAT imposed in Secs. 106 to 108 of the Tax Code.
>
> xxx xxx xxx
>
> ***'Taxable sale'*** refers to the **sale, barter, exchange and/or lease of goods or properties, including transactions 'deemed sale' and the performance of service for a consideration, whether in cash or in kind**, all of which are subject to tax under Secs. 106 to 108 of the Tax Code.
>
> SEC. 4.105-2. *Nature and Characteristics of VAT.* - **VAT is a tax on consumption levied on the sale, barter, exchange or lease of goods or properties and services in the Philippines and on importation of goods into the Philippines.** The seller is the one statutorily liable for the payment of the tax but the amount of the tax may be shifted or passed on to the buyer, transferee or lessee of the goods, properties or services. This rule shall likewise apply to existing contracts of sale or lease of goods, properties or services at the time of the effectivity of RA No. 9337. However, in the case of importation, the importer is the one liable for the VAT."*(Emphasis supplied)*

Interest income on savings deposit is passive income and as such, is neither sale of goods nor sale of services. Further, transactions deemed sale mentioned in Section 4.105-1 of RR No. 16-2005, in relation to Section 106(B) of the NIRC of 1997, do not include interest income. In fact, there is no provision under Revenue Regulations No. 16-2005 which states that such interest income on savings deposit is subject to VAT.

Thus, for lack of legal basis, the deficiency VAT assessment on interest income shall be cancelled.

3. Miscellaneous Income - P142,234.00

Respondent maintains that upon verification of petitioner's documents, records disclosed that among the Miscellaneous Income declared were collection of proceeds on copra harvest, a VAT-exempt transaction. However, respondent found that petitioner failed to register such business activity as additional line of business and a VAT invoice was issued. Hence, petitioner was assessed with regular VAT, pursuant to Section 4.113-4 of RR No. 16-2005.

Petitioner claims that out of the amount of P142,234.00 as Miscellaneous Income, the income from copra sales proceeds for the first three (3) quarters of calendar year 2005 amounts to only P59,752.00. On the other hand, the amount of P79,772.86 included as Miscellaneous Income came from collection of land amortization for 2004.

Petitioner submitted the Details of Other Income[59] reported in its Audited Financial Statements and Annual Income Tax Return for 2005, to wit:

Date	Particulars	OR #	Total	Copra Maasim	Land Amortization	Others
1/17/2005	Collections on proceeds of copra harvest at Maasim	1044	P 20,942.00	P 20,942.00		
4/21/2005	Collections on proceeds of copra harvest at Maasim	1060	19,408.00	19,408.00		
5/30/2005	Disca land amortization payment for the year 2004	1068	79,772.86		P 79,772.86	
7/25/2005	Collections on proceeds of copra harvest at Maasim	1083	19,402.00	19,402.00		
12/29/2005	Bank credit memo not yet taken up in the books		546.25			P 546.25
12/29/2005	Ck#23543 overstated by the book		125.93			125.93
12/29/2005	Realized forex gain on paid accruals	U80	2,037.20			2,037.20
	TOTAL		**P142,234.24**	**P59,752.00**	**P 79,772.86**	**P2,709.38**

[59] Exhibit "OO", Docket, p. 1528.

As can be gleaned from the above table, it appears that the income from the copra harvest amounts to P59,752.00. In support thereof, petitioner submitted the official receipts[60] it issued for the collection of proceeds of copra harvest. Evaluation of the same revealed that, indeed, petitioner failed to display prominently on the receipt the words "VAT-exempt sale". Thus, petitioner shall be held liable to pay VAT thereon.

As to the remaining Miscellaneous Income of P82,482.24 allegedly pertaining to the collection of land amortization for 2004 in the amount of P79,772.86 and Other Income of P2,709.38, petitioner did not provide documents other than its schedule, which this Court finds as self-serving to support the claim and to disprove that the same do not pertain to the collection of proceeds of copra harvest. Consequently, the entire Miscellaneous Income in the amount of P142,234.00 being assessed by respondent shall be subject to VAT.

4. Disallowed Input Tax - P25,500.05

Respondent found that input taxes for 2005 amounting to P25,500.05 are not properly substantiated. Considering that petitioner did not submit invoices or official receipts to disprove respondent's findings, the disallowance shall be upheld.

In fine, petitioner's basic deficiency VAT amounts to **P87,753.58**, computed as follows:

Taxable Sales/Receipts per Return		P5,664,672.95
Add: Discrepancies per Investigation:		
1. Rental Income - Not Subjected to Value Added Tax	P 680,502.05	
2. Miscellaneous Income	142,234.00	822,736.05
Taxable Sales/Receipts per Investigation		P6,487,409.00
Output Tax Due		P 648,740.90
Less: Creditable Input Tax Per Return	P 212,813.71	
Less: Unsubstantiated Input Tax	25,500.05	187,313.66
Deficiency Value Added Tax Due		P 461,427.24
Less: Tax Withheld / Paid Per Return		373,673.66
Basic Deficiency VAT		**P 87,753.58**

[60] Exhibits "OO-1" to "OO-3", Docket, pp. 1529-1530.

III. COMPROMISE PENALTY

Considering that there is no showing that petitioner voluntarily entered into a compromise agreement with respondent, the compromise penalty of P92,000.00 shall be cancelled.

WHEREFORE, in view of the foregoing considerations, the instant Petition for Review is hereby **PARTIALLY GRANTED**. The assessments for deficiency income tax and value-added tax issued by respondent against petitioner for taxable year 2005 are hereby **AFFIRMED** with some modifications. Accordingly, petitioner is hereby **ORDERED** to **PAY** respondent the modified amount of P403,468.34, inclusive of the twenty-five percent (25%) surcharge imposed under Section 248(A)(3) of the NIRC of 1997, as amended, computed as follows:

Deficiency Tax	Basic	25% Surcharge	Total
Income Tax	P 235,021.09	P 58,755.27	P 293,776.36
VAT	87,753.58	21,938.40	109,691.98
Total Tax Due	**P322,774.67**	**P80,693.67**	**P403,468.34**

Moreover, petitioner is **ORDERED** to **PAY** (a) deficiency interest at the rate of twenty percent (20%) *per annum* on the basic deficiency income tax of P235,021.09 and value-added tax of P87,753.58 computed from April 15, 2006 and January 25, 2006, respectively, until full payment thereof pursuant to Section 249(B) of the NIRC of 1997, as amended; and (b) delinquency interest at the rate of 20% *per annum* on the total amount of P403,468.34 and on the 20% deficiency interest which have accrued as aforestated in (a), computed from July 29, 2009 until full payment thereof pursuant to Section 249(C) of the NIRC of 1997, as amended.

The compromise penalty of P92,000.00 is hereby **CANCELLED** as there is no compromise agreement between the parties.

SO ORDERED.

ERLINDA P. UY
Associate Justice

I CONCUR:

ESPERANZA R. FABON-VICTORINO
Associate Justice

ATTESTATION

I attest that the conclusions in the above Decision were reached on consultation before the case was assigned to the writer of the opinion of the Court's Division.

ERLINDA P. UY
Associate Justice
Chairperson

CERTIFICATION

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

ROMAN G. DEL ROSARIO
Presiding Justice