REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

SECOND DIVISION

ROCA SECURITY AND INVESTIGATION AGENCY, INC.,
Petitioner,

- versus-

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

CTA Case No. 8718

Members:

Castañeda, Jr., *Chairperson*
Casanova, and
Cotangco-Manalastas, *JJ.*

Promulgated:

JUL 2 1 2016

10:50 a.m.

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DECISION

COTANGCO-MANALASTAS, *J.:*

The case involves the Petition for Review filed by Roca Security and Investigation Agency, Inc. for the cancellation and withdrawal of the Formal Letter of Demand and Assessment Notices issued by the Commissioner of Internal Revenue, assessing the former for alleged tax deficiencies, compromise penalties and surcharges in the aggregate amount of ₱8,679,693.85 for taxable year 2009.[1]

FACTS

Petitioner Roca Security and Investigation Agency, Inc. is a corporation duly organized and existing under and by virtue of the laws of the Republic of the Philippines,[2] with business address at 1716 Honradez St., Barangay 437, Sampaloc, Manila.[3] It is a registered taxpayer under Certificate of

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[1] Par. I, Summary of the Case, Pre-Trial Order, docket, vol. I, p. 181.
[2] Exhibit "P-1", docket, vol. I, p. 274; now known as Roca Security Services, Inc.
[3] Par. 1, Petition for Review, docket, vol. I, p. 6.

Registration No. OCN 1RC0000253629, with Taxpayer Identification No. (TIN) 000-085-243-000.[4]

On the other hand, respondent is the duly appointed Commissioner of the Bureau of Internal Revenue (BIR) vested under the appropriate laws with the authority to carry out the functions, duties and responsibilities of said office, including, *inter alia*, the power to decide disputed assessments and cancel and abate tax liabilities, pursuant to the provisions of the National Internal Revenue Code (NIRC) of 1997 and other tax laws, rules and regulations. She holds office at the BIR National Office Building, Agham Road, Diliman, Quezon City.

On April 15, 2010, petitioner filed its Annual Income Tax Return (ITR) for taxable year 2009.[5]

On September 17, 2010, petitioner received the electronic Letter of Authority No. 201000013736[6] together with the First Request for Presentation of Records. The Second Request and Final Request for Presentation of Records were likewise received by petitioner.[7]

A Subpoena Duces Tecum with No. RR6-2012-0228 was issued on May 16, 2012, commanding petitioner to appear before the BIR and to submit its books of accounts and other accounting records for taxable year 2009.[8]

On October 12, 2012, respondent sent to petitioner a Post Reporting Notice with Details of Computation, which informed the latter of its tax liability.[9]

On March 25, 2013, respondent issued a Preliminary Assessment Notice (PAN) against petitioner for alleged income tax deficiency amounting to ₱7,719,617.21 and deficiency improperly accumulated earnings tax (IAET) amounting to ₱960,076.64, including increments, for taxable year ending

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[4] Exhibit "P-11", docket, vol. I, p. 311.
[5] Exhibit "P-5", docket, vol. I, pp. 294 to 295.
[6] Exhibit "R-1", docket, vol. II, p. 617.
[7] Par. 3, Facts Admitted, Joint Stipulation of Facts and Issues (JSFI), docket, vol. I, p. 171. The date was erroneously written in the JSFI as "17 September 2007", instead of September 17, 2010.
[8] Par. 4, Facts Admitted, JSFI, docket, vol. I, p. 172.
[9] Exhibit "R-3", docket, vol. II, pp. 619 to 620, BIR records, pp. 143 to 144.

December 31, 2009; which petitioner received on April 3, 2013.[10]

As a result, petitioner filed a Letter Protest on April 18, 2013 assailing the PAN.[11]

Despite the filing of the said protest letter, a Formal Letter of Demand (FLD) with Details of Discrepancies and Assessment Notices (FAN) with Nos. 32-09-IT-4995 and 32-09-IAET-4996 were issued on April 12, 2013.[12] Petitioner received the FLD and the FAN on April 19, 2013.[13]

Petitioner disputed the said FLD and FAN on May 16, 2013.[14]

Respondent issued a letter dated September 10, 2013, affirming the assessed tax deficiencies due to the alleged failure of petitioner to submit relevant documents in support of its protest and stating that this is their Final Decision on the Disputed Assessment (FDDA).[15]

Consequently, petitioner filed the present Petition for Review[16] before this Court on October 9, 2013.

In the Answer[17] filed on November 20, 2013, respondent raised the following special and affirmative defenses:

> "9. **RESPONDENT** hereby adopts by way of reference all of the allegations in the foregoing paragraphs insofar as the same are material and relevant, and alleges that:

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[10] Par. 5, Admitted Facts, JSFI, docket, vol. I, p. 172; Exhibits "P-7" and "P-7-A", docket, vol. I, p. 303 and pp. 304 to 305, respectively; Exhibits "R-7", docket, vol. II, pp. 623 to 625.

[11] Par. 6, Admitted Facts, JSFI, docket, vol. I, p. 172; Exhibit "P-2", docket, vol. I, pp. 285 to 287; Exhibit "R-13", docket, vol. II, pp. 632 to 634. The parties stipulated the date of filing as April 18, 2013. However, the date (of receipt) stamped on the PAN was April 17, 2013.

[12] Exhibits "P-8", "P-9", and "P-10", docket, vol. I, pp. 306 to 308, p. 309 and p. 310, respectively; Exhibits "R-8", "R-9", and "R-10", docket, vol. II, p. 626, p. 627 and pp. 628 to 630, respectively.

[13] Par. 7, Admitted Facts, JSFI, docket, vol, I, p. 172.

[14] Par. 8, Admitted Facts, JSFI, docket, vol. I, p. 172; Exhibit "P-3", docket, vol. I, pp. 289 to 291; Exhibit "R-14", docket, vol. II, pp. 635 to 637.

[15] Par. 9, Admitted Facts, JSFI, docket, vol. I, p. 172; Exhibit "P-4", docket, vol. I, p. 293; Exhibits "R-11" and "R-18", docket, vol. II, p. 631 and p. 642, respectively.

[16] Docket, vol. I, pp. 6 to 16.

[17] Docket, vol. I, pp. 38 to 43.

10. Under Section 228 of the Tax Code of 1997, as amended, a tax assessment maybe administratively protested by filing a request for reinvestigation or reconsideration within 30 days from receipt of the assessment notice. Within sixty (60) days from the filing of the protest, all relevant supporting documents shall have been submitted; otherwise, the assessment shall become final;

11. In the instant case, while a protest on the assessment was indeed filed on 16 May 2013, the petitioner, however, failed to submit relevant supporting documents in support of its protest;

12. Therefore, considering that petitioner failed to submit documents in support of its protest, the Final Assessment Notice (FAN) Nos. 32-09-IT-4995 and 32-09-IAET-4996 have become final, executory and demandable. Accordingly, the said assessment ceases to be a disputed assessment and thus, the legality and validity thereof can no longer be the subject of a judicial inquiry in the instant Petition for Review *(La Flor Dela Isabela, Inc. vs. CIR, CTA Case No. 7709, 09 June 2010)*;

13. Petitioner likewise claimed that the subject FANs are void because they failed to provide the factual and legal bases of the assessment as required under Section 228 of the NIRC, as amended and Revenue Regulation No. 12-99. Contrary thereto, however, petitioner was duly informed of the facts and law upon which the subject assessments were based;

14. Section 228 of the NIRC, as amended, and RR No. 12-99 merely require that the taxpayer must be informed in writing of the law and the facts on which the assessment was made. Thus, there was compliance with the mandate of the law when the FAN is accompanied with complete details, such as the computations, schedules, and applicable laws, which are the factual and legal bases covering the aforementioned discrepancies established during the investigation. *[Irene C. Salud vs. CIR, CTA EB Case No. 412 (CTA Case No. 6954), 30 April 2009]*

15. Moreover, there is no merit to the petitioner's claim that the subject assessments were void because the three year prescriptive period mandated by law in issuing assessment had already lapsed;

16. Well-settled is the rule that it is not the issue date of the demand letter and/or notice of assessment that is the reckoning point in prescription; but rather, it is the date

when the said demand letter or notice is released, mailed or sent to the taxpayer that constitutes actual assessment. As long as the release thereof is effected before prescription sets in, the assessment is deemed made on time even though the same is actually received by the taxpayer after the expiration of the prescriptive period *(Republic vs. de Guzman, 5 SCRA 990; Basilan Estates vs. CIR, 21 SCRA 17)*;

17. Here, the subject assessments notices were mailed to the petitioner's registered address on 12 April 2013 and duly received by the petitioner on 19 April 2013; thus, based on the above-cited jurisprudence, it is clear that prescription has not set in;

18. Finally, the subject assessments are valid and correct and the petitioner has the burden of proof to impugn their validity *(Behn Meyer & Co. vs. Collector of Internal Revenue, 27 Phil. 647)*. Thus, similarly held, tax assessments by examiners are presumed correct and made in good faith and the taxpayer has the duty to prove otherwise *(Commissioner of Internal Revenue vs. Construction Resources of Asia, Inc., 145 SCRA 671)*; and assessments duly made by the BIR examiner and approved by her superior officers will not be disturbed *(Gutierrez vs. Villegas, 8 SCRA 547)*;

19. The burden of proof is on the taxpayer contesting the validity or correctness of an assessment to prove not only that the Commissioner of Internal Revenue is wrong but also that the taxpayer is right *(Tan Guan vs. Court of Tax Appeals, et al., 19 SCRA 903 [1967]; Collector of Internal Revenue vs. Bohol Land Transportation Co., 107 Phil. 967 [1960])*;

20. All presumptions are in favor of the correctness of the assessment made by the Commissioner of Internal Revenue; the taxpayer must prove the contrary *(Commissioner of Internal Revenue vs. Antonio Tuason, Inc. 173 SCRA 397; Commissioner of Internal Revenue vs. Construction Resources of Asia, Inc., 145 SCRA 671)*;

21. The assessments were issued in the regular course and within the reglementary period to assess provided for by law."

Petitioner's Pre-Trial Brief[18] and Respondent's Pre-Trial Brief[19] were filed on January 13, 2014 and January 14, 2014, respectively.

[18] Docket, vol. I, pp. 61 to 67.
[19] Docket, vol. I, pp. 105 to 109.

Upon motion of petitioner,[20] the Court commissioned Mr. Glenn Ian D. Villanueva as the Independent Certified Public Accountant (ICPA) for the case on February 17, 2014.[21]

The parties submitted their Joint Stipulation of Facts and Issues[22] on February 20, 2014. Then on February 27, 2014, the Court approved the same and terminated the pre-trial.[23]

During trial, petitioner presented Atty. Giovanni Bautista and Mr. Glenn Ian D. Villanueva as witnesses.[24] Thereafter, petitioner formally offered Exhibits "P-1" to "P-22", inclusive of sub-markings, which were all admitted except for Exhibit "P-1-a".[25]

On the other hand, respondent presented Revenue Officers Benilda R. Sanchez, Allan C. Quizon, Jay F. Faustino, and Armando C. Macatangay as witnesses.[26] Then, Exhibits "R-1" to "R-26", including the sub-markings, were formally offered by respondent. All of the said exhibits were later admitted in evidence.[27]

This case was declared submitted for decision on August 27, 2015,[28] considering the Memorandum for the Petitioner[29] filed through registered mail on July 27, 2015 and received by the Court on July 30, 2015, and Respondent's Memorandum[30] filed on August 25, 2015.

ISSUES

The parties presented the following issues[31] for the Court's determination:

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[20] Motion for the Appointment of an Independent Certified Public Accountant, docket, vol. I, pp. 156 to 158.
[21] Minutes of the Hearing dated February 17, 2014, docket, vol. I, p. 169.
[22] Docket, vol. I, pp. 171 to 179.
[23] Pre-Trial Order, docket, vol. I, pp. 181 to 186.
[24] Minutes of the Hearing dated March 17, 2014, May 5, 2014, June 2, 2014 and July 7, 2014, docket, vol. I, p. 187, p. 236, p. 260 and p. 264, respectively.
[25] Resolutions dated October 22, 2014 and October 29, 2014, docket, vol. II, pp. 531 to 532 and p. 535, respectively.
[26] Minutes of the Hearing dated October 29, 2014, November 17, 2014, March 16, 2015 and April 27, 2015, docket, vol. II, p. 533, p. 553, p. 598 and p. 604, respectively.
[27] Resolution dated June 24, 2015, docket, vol. II, pp. 662 to 663.
[28] Resolution, docket, vol. II, p. 697.
[29] Docket, vol. II, pp. 664 to 678.
[30] Docket, vol. II, pp. 684 to 696.
[31] Issues, JSFI, docket, vol. I, pp. 173 to 174.

1. Whether the Court has jurisdiction to entertain the instant petition for review;

2. Whether Assessment Notice No. 32-09-IT-4995 and Assessment Notice No. 32-09-IAET-4996 have become final and demandable;

3. Whether petitioner is liable to pay an income tax deficiency in the amount of ₱7,759,477.00 for the year December 31, 2009;

4. Whether petitioner is liable to pay improperly accumulated earnings tax deficiency in the amount of ₱964,361.10 for the year ending December 31, 2009;

5. Whether Assessment Notice No. 32-09-IT-4995 dated April 12, 2013 representing alleged income tax deficiency and Assessment Notice No. 32-09-IAET-4996 dated April 12, 2013 representing alleged IAET have already prescribed pursuant to Section 203 of the 1997 Tax Code; and

6. Whether respondent failed to inform petitioner about the facts and laws upon which the present assessment is made.

The above-enumerated issues can be summarized into two main issues, to wit:

1. Whether this Court has jurisdiction over the present petition for review; and

2. Whether petitioner is liable to pay income tax deficiency in the amount of ₱7,759,477.00 and IAET deficiency in the amount of ₱964,361.10 for taxable year 2009.

DISCUSSION/RULING

Petitioner contends that after the receipt of the FDDA, it promptly filed the instant petition for review. Petitioner likewise claims that the subject assessment is a jeopardy assessment in violation of its right to due process; thus, the assessment is void.

Further, petitioner asserts that the assessment was issued beyond the period prescribed under Section 203 in relation to Section 114(A) of the NIRC of 1997, as amended.

Respondent counter-argues that petitioner failed to submit documents in support of the protest. As such, the FAN issued in connection with the subject deficiency tax assessment is now final, executory and demandable. Respondent alleges that since the subject assessment became final and executory, it is no longer appealable to this Court.

Respondent likewise asserts that the FAN was issued within the prescriptive period and the same informed petitioner of the facts and the law upon which the subject assessment was based.

Section 228 of the NIRC of 1997, as amended, provides:

> "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."

In relation thereto, Section 203 of the NIRC of 1997, as amended, states:

"SEC. 203. *Period of Limitation Upon Assessment and Collection.* – Except as provided in Section 222, internal revenue taxes shall be assessed within three (3) years after the last day prescribed by law for the filing of the return, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period: *Provided,* That in a case where a return is filed beyond the period prescribed by law, the three (3)-year period shall be counted from the day the return was filed. For purposes of this Section, a return filed before the last day prescribed by law for the filing thereof shall be considered as filed on such last day."

Furthermore, in the case of *Barcelon, Roxas Securities, Inc. (now known as UBP Securities, Inc.) vs. Commissioner of Internal Revenue*[32], the Supreme Court held that:

"Under Section 203 of the National Internal Revenue Code (NIRC), respondent had three (3) years from the last day for the filing of the return to send an assessment notice to petitioner. In the case of *Collector of Internal Revenue v. Bautista,* this Court held that **an assessment is made within the prescriptive period if notice to this effect is released, mailed or sent by the CIR to the taxpayer within said period.** Receipt thereof by the taxpayer within the prescriptive period is not necessary. At this point, **it should be clarified that the rule does not dispense with the requirement that the taxpayer should actually**

[32] G.R. No. 157064, August 7, 2006.

> **receive, even beyond the prescriptive period, the assessment notice which was timely released, mailed and sent.**" (*Emphasis supplied*)

After careful evaluation of the records, the Court finds that respondent's right to assess petitioner for deficiency taxes has not yet prescribed.

Petitioner filed its Annual Income Tax Return[33] on April 15, 2010 for taxable year 2009, or the last day prescribed by law for its filing. Accordingly, respondent had three years from April 15, 2010 or until April 15, 2013 within which to assess petitioner.

Respondent released the FLD with Details of Discrepancies and FAN Nos. 32-09-IT-4995 and 32-09-IAET-4996 to the Central Post Office in Manila for mailing on April 12, 2013[34], which petitioner received on April 17, 2013.[35]

It is clear from the foregoing that the FLD and the FAN were issued within the three-year prescriptive period.

As regards the allegations of respondent that the assessment has become final and executory due to failure of petitioner to submit documents supporting the protest, the Court finds it without merit.

In the case of *Commissioner of Internal Revenue vs. First Express Pawnshop Company Inc.*,[36] the Supreme Court explained that the term "relevant supporting documents" are those documents necessary to support the legal basis in disputing a tax assessment *as determined by the taxpayer.* The BIR can only inform the taxpayer to submit additional documents but cannot demand what type of supporting documents should be submitted. Otherwise, a taxpayer will be at the mercy of the BIR, which may require the production of documents that a taxpayer cannot submit.

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[33] Exhibit "P-5", docket, vol. I, pp. 294 to 295.

[34] Exhibits "R-20" and "R-20-a", docket, vol. II, p. 647; Exhibits "R-22" and "R-22-a", docket, vol. II, p. 652.

[35] Exhibits "R-24" and "R-24-a", docket, vol. II, p. 656. The Registry Return Receipt showed that the FAN was delivered on April 17, 2013. However, parties stipulated that petitioner received the FAN on April 19, 2013; see par. 7, Admitted Facts, JSFI, docket, p. 172.

[36] G.R. Nos. 172045-46, June 16, 2009.

Moreover, as early as March 12, 2012, petitioner informed respondent that the former's accounting records and books of accounts for taxable year 2009 were destroyed due to the flood brought about by typhoon Ondoy on September 26, 2009.[37] Respondent was aware that petitioner did not intentionally omit the submission of its supporting documents.

With respect to the allegation that Assessment Notice No. 32-09-IT-4995 and Assessment Notice No. 32-09-IAET-4996 are void for failure to state the facts and laws upon which the assessments were made, the same has no basis.

A thorough evaluation of the FLD and the FAN shows that they contained the facts and laws upon which the assessments were based in accordance with Section 3.1.4 of Revenue Regulations (RR) No. 12-99.

The instant petition for review was filed on October 9, 2013. However, it is not clear from the records when the FDDA was received by petitioner. Nevertheless, even counting from the earliest possible date that petitioner could have received the same, *i.e.*, date FDDA was issued on September 10, 2013, the petition for review was filed within the thirty-day appeal period, hence, this Court has jurisdiction over the case.

The Court shall now proceed to determine whether petitioner is liable to pay deficiency income tax in the amount of ₱7,759,477.00 and deficiency IAET in the amount of ₱964,361.10 for taxable year 2009.

The subject FLD and FAN assessed petitioner for deficiency taxes in the aggregate amount of ₱8,723,838.62, including surcharge and interest, for taxable year 2009, summarized as follows:

Tax Type	Basic Tax	Surcharge	Interest	Total
Income tax	₱ 4,849,673.45	₱ -	₱ 2,909,804.07	₱ 7,759,477.52
IAET	521,276.27	130,319.07	312,765.76	964,361.10
Total	**₱5,370,949.72**	**₱130,319.07**	**₱3,222,569.83**	**₱8,723,838.62**

The Court will discuss these items in *seriatim*.

[37] BIR records, pp. 130 to 131.

I. Deficiency Income Tax

Respondent assessed petitioner for basic deficiency income tax in the amount of ₱4,849,673.45, computed as follows:[38]

Taxable Net Income per ITR		₱ 1,266,967.95
Add: Adjustments		
50% Disallowed Operating exp. – unsupported/ no schedule	₱ 196,147.59	
100% Disallowed Cost of Service & Operating Exp. – non-withholding	15,969,430.61	16,165,578.20
Adjusted taxable net income		17,432,546.15
Income Tax due		5,229,763.84
Less: Payments/tax credit		380,090.39
Deficiency Income Tax		**₱4,849,673.45**

The Court will delve into the propriety of the expense deductions disallowed by respondent, namely:

a. Unsupported operating expenses	₱ 196,147.59
b. Cost of services and operating expenses not subjected to withholding tax	₱15,969,430.61

a. Unsupported operating expenses – ₱196,147.59

Respondent disallowed fifty percent (50%) of petitioner's operating expenses, as detailed below, for allegedly being unsupported/no schedule.[39] Petitioner was assessed based on the Best Evidence Obtainable Rule pursuant to Section 6(B)[40] of the NIRC of 1997, as amended, and Revenue Memorandum Circular (RMC) No. 23-2000.[41]

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[38] Exhibit "P-8", docket, vol. I, p. 306.

[39] Annex A of Exhibit "P-8", docket, vol. I, p. 308.

[40] SEC. 6. *Power of the Commissioner to Make Assessments and Prescribe Additional Requirements for Tax Administration and Enforcement.* –
xxx
(B) *Failure to Submit Required Returns, Statements, Reports and other Documents.* - When a report required by law as a basis for the assessment of any national internal revenue tax shall not be forthcoming within the time fixed by laws or rules and regulations or when there is reason to believe that any such report is false, incomplete or erroneous, the Commissioner shall assess the proper tax on the best evidence obtainable.
In case a person fails to file a required return or other document at the time prescribed by law, or willfully or otherwise files a false or fraudulent return or other document, the Commissioner shall make or amend the return from his own knowledge and from such information as he can obtain through testimony or otherwise, which shall be *prima facie* correct and sufficient for all legal purposes.

[41] Respondent's Memorandum, docket, vol. II, p. 693; Exhibit "P-8", docket, vol. I, p. 306.

Operating Expense	Amount	50% Thereof
Representation & entertainment	₱ 18,205.00	₱ 9,102.50
Taxes and licenses	51,670.94	25,835.47
Transportation expense	72,670.38	36,335.19
Communication expense	70,421.75	35,210.88
Gasoline & oil	125,283.07	62,641.54
Insurance & bonds	6,055.83	3,027.92
Office supplies	47,988.20	23,994.10
Total		**₱196,147.59**

Petitioner has manifested that it would submit documents during trial that would support and justify its operating expenses.[42] However, petitioner failed to do so. Nothing was offered to controvert respondent's assessment regarding the unsupported operating expenses.[43] Petitioner argues that it was never afforded sufficient amount of time to produce the documents required by the revenue examiners to refute the disallowance.[44]

The Court is not convinced.

Petitioner received the PAN dated March 25, 2013 on April 3, 2013[45], giving petitioner 15 days from receipt (or until April 18, 2013) to respond. Petitioner was able to file its response to the PAN on April 17, 2013.[46] Thereafter, on April 17, 2013[47], petitioner received the FLD and FAN dated April 12, 2013[48] and was able to protest the same on May 16, 2013[49].

Based on the foregoing, the period from April 3, 2013, or from the time the PAN was received by petitioner, up to July 15, 2013[50], or the deadline for submitting relevant supporting

[42] Par. 16, Petition for Review, docket, vol. I, p. 10.

[43] Formal Offer of Evidence, docket, vol. I, pp. 266 to 273.

[44] Par. 15, Petition for Review, docket, vol. I, p. 10; par. 18, Memorandum for the Petitioner, docket, vol. II, p. 670.

[45] Par. 5, Admitted Facts, JSFI, docket, vol. I, p. 172; Exhibits "P-7" and "P-7-A", docket, vol. I, p. 303 and pp. 304 to 305, respectively; Exhibits "R-7", docket, vol. II, pp. 623 to 625.

[46] Par. 6, Admitted Facts, JSFI, docket, vol. I, p. 172; Exhibit "P-2", docket, vol. I, pp. 285 to 287; Exhibit "R-13", docket, vol. II, pp. 632 to 634. The parties stipulated the date of filing as April 18, 2013. However, the date (of receipt) stamped on the PAN was April 17, 2013.

[47] Exhibits "R-24" and "R-24-a", docket, vol. II, p. 656. The Registry Return Receipt showed that the FAN was delivered on April 17, 2013. However, parties stipulated that petitioner received the FAN on April 19, 2013; see par. 7, Admitted Facts, JSFI, docket, vol. I, p. 172.

[48] Exhibits "P-8", "P-9", and "P-10", docket, vol. I, pp. 306 to 308, p. 309 and p. 310, respectively; Exhibits "R-8", "R-9", and "R-10", docket, vol. II, p. 626, p. 627 and pp. 628 to 630, respectively.

[49] Par. 8, Admitted Facts, JSFI, docket, p. 172; Exhibit "P-3", docket, vol. I, pp. 289 to 291; Exhibit "R-14", docket, vol. II, pp. 635 to 637.

[50] Protest was filed on May 16, 2013; counting 60 days therefrom, petitioner had until July 15, 2013 within which to submit supporting documents.

documents provided in Section 228 of the NIRC of 1997, as amended, is sufficient time to gather necessary supporting documents to prove petitioner's entitlement to the deduction of its operating expenses from its taxable gross income.

Since petitioner's claimed deductions are not supported by documentary evidence, the Court deems it appropriate to uphold respondent's disallowance, applying the 50% rule of approximation provided under Section 2.4(c) of RMC No. 23-2000, which cited the case of *Zamora vs. Collector of Internal Revenue*[51]. Quoted hereunder is the pertinent part of RMC No. 23-2000:

> "(c) *Assessment Based on Estimate; 50% Rule, in the Absence of Receipts to Prove Actual Amount of Expense Deduction.* — The Court held in the Mariano Zamora case that, if there is a showing that expenses have been incurred but the exact amount thereof cannot be ascertained due to absence of documentary evidence, it is the duty of the BIR to make an estimate of the deduction that may be allowable in computing the taxpayer's taxable income, bearing heavily against the taxpayer whose inexactitude is of his own making. That disallowance of 50% of the taxpayer's claimed deduction is valid."

Thus, the disallowance of petitioner's operating expenses is upheld. Accordingly, petitioner's deductions from its taxable gross income for the year 2009 in the amount of ₱196,147.59 shall be disallowed.

b. Cost of services and certain operating expenses not subjected to withholding tax - ₱15,969,430.61

Respondent's audit disclosed that petitioner failed to withhold taxes on its cost of services and certain operating expenses, thereby warranting disallowance; the breakdown of which is as follows:[52]

[51] *Mariano Zamora vs. Collector of Internal Revenue and Court of Tax Appeals,* G.R. No. L-15290; *Collector of Internal Revenue vs. Mariano Zamora,* G.R. No. L-15280; *Esperanza A. Zamora, as Special Administratrix of the Estate of Felicidad Zamora vs. Collector of Internal Revenue and Court of Tax Appeals,* G.R. No. L-15289; *Collector of Internal Revenue vs. Esperanza A. Zamora, as Special Administratrix, etc.,* G.R. No. L-15281, all dated May 31, 1963.

[52] Annex A of Exhibit "P-8", docket, vol. I, p. 308.

1. Cost of services	₱ 15,855,730.76
2. Ammunition and training	15,255.38
3. Utilities	82,736.95
4. Repair and maintenance	15,707.52
Total	**₱15,969,430.61**

b.1. Cost of services

As can be gleaned from the above table, the bulk of the disallowance can be traced to the cost of services.

Petitioner admits that it is mandated to impose withholding taxes on the salaries of the security guards pursuant to RMC No. 39-2007,[53] which provides that:

> "The Security Agency who is the trustee of the funds segregated and earmarked as salaries of the security guards is the withholding agent for purposes of the withholding tax on compensation income. xxx"

However, petitioner contends that its security guards are minimum wage earners (MWE) as defined under Section 2.78.1(B)(13) of RR No. 2-98, as amended by RR No. 10-2008, quoted hereunder:

> "(B) *Exemptions from Withholding Tax on Compensation.* – The following income payments are exempted from the requirements of withholding tax on compensation:
>
> xxx xxx xxx
>
> (13) Compensation income of MWEs who work in the private sector and being paid the Statutory Minimum Wage (SMW), as fixed by Regional Tripartite Wage and Productivity Board (RTWPB)/National Wages and Productivity Commission (NWPC), applicable to the place where he/she is assigned.
>
> The aforesaid income shall likewise be exempted from income tax."

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[53] Par. 19, Petition for Review, docket, vol. I, p. 12; par. 21, Memorandum for the Petitioner, docket, vol. II, p. 672.

Petitioner insists that it is not obligated to withhold on the compensation paid to security guards; thus, the disallowance of cost of services amounting to ₱15,855,730.76 must be cancelled and withdrawn.

The Court finds petitioner's contention partly meritorious.

Petitioner is engaged in rendering protective and security services to industrial and commercial establishments, private properties and government properties.[54] Undoubtedly, its cost of services represents monies received from its clients to pay for the security guards' salaries.[55]

Based on the Revised Report[56] of the Court-commissioned ICPA, the gross pay of petitioner's security guards for taxable year 2009 totaled to ₱38,876,891.08, which when compared with the cost of services of ₱15,855,730.76 reflected per petitioner's 2009 Audited Financial Statements[57]/Annual Income Tax Return[58] reveals a discrepancy of ₱23,021,160.32, as shown below:[59]

	Reference	**Amount**
Cost of Services Per 2009 Audited Financial Statements	*Exhibit P-6, Page 8*	**₱ 15,855,730.76**
Cost of Services Per 2009 Schedule of Security Guards' Salary		
Total Gross Pay-January 2009	*Exhibit P-12, Page 8*	₱ 3,183,878.21
Total Gross Pay-February 2009	*Exhibit P-12, Page 17*	2,821,762.66
Total Gross Pay-March 2009	*Exhibit P-12, Page 25*	3,113,100.19
Total Gross Pay-April 2009	*Exhibit P-12, Page 34*	3,062,923.69
Total Gross Pay-May 2009	*Exhibit P-12, Page 43*	3,015,316.91
Total Gross Pay-June 2009	*Exhibit P-12, Page 52*	3,029,121.14
Total Gross Pay-July 2009	*Exhibit P-12, Page 62*	3,196,720.02
Total Gross Pay-August 2009	*Exhibit P-12, Page 70*	3,035,421.02
Total Gross Pay-September 2009	*Exhibit P-12, Page 80*	3,015,505.06
Total Gross Pay-October 2009	*Exhibit P-12, Page 90*	3,076,625.01
Total Gross Pay-November 2009	*Exhibit P-12, Page 99*	2,984,367.20
Total Gross Pay -December	*Exhibit P-12, Page 109*	3,199,025.29
Total 13th Month Pay	*Annex 14*	2,143,124.68
Total		**₱ 38,876,891.08**
Discrepancy-Amount per Audited Financial Statements is (under)/over		**₱(23,021,160.32)**

[54] BIR records, p. 21.
[55] Par. 18, Petition for Review, docket, vol. I, p. 11; Par. 20, Memorandum for the Petitioner, docket, vol. II, p. 671; Par. B.1, p. 3 of Exhibit "P-14"; A34, Amended Judicial Affidavit of Atty. Giovanni Bautista, docket, vol. II, p. 516.
[56] Exhibit "P-14".
[57] Exhibit "P-6", docket, vol. I, p. 300.
[58] Line 18C, Exhibit "P-5", docket, vol. I, p. 294.
[59] P. 4 of Exhibit "P-14".

Notwithstanding that the ICPA was unable to account for the aforesaid difference, it should be noted that only ₱15,855,730.76 was claimed by petitioner as deduction from its gross income. Further, the unaccounted difference was not claimed as allowable deduction from petitioner's taxable gross income.

Out of the total gross pay, only ₱35,313,099.19 is supported by pay slips, cash deposit slips, remittance forms, *etc.*[60], as summarized by the ICPA in *Annex 1* of his revised report[61].

The supporting schedules[62] of *Annex 1* detailed, among others, the daily wage rate per company and statutory minimum wage (SMW) per wage order[63] (issued by Regional Tripartite and Wage Productivity Board).

A perusal of the schedules shows that not all of petitioner's security guards are paid at or below SMW, wherein the corresponding salaries of which aggregate to ₱10,907,168.43, broken down below:

Region	**Annex (*Exhibit "P-14"*)**	**Gross Pay**
At or below SWM		
National Capital Region	2	₱ 5,896,797.89
Ilocos Region (Region 1)	4	30,857.36
Calabarzon Growth Corridor Area (Region 4-A; Cainta and Imus)	7-1	2,940,262.10
Calabarzon Growth Corridor Area (Region 4-A; Antipolo, Calamba and Sta. Rosa, Laguna)	7-2	1,535,039.88
Calabarzon Emerging Growth Area (Region 4-A; Batangas)	7-3	50,427.45
Western Visayas (Region 6)	9	16,950.64
Central Visayas (Region 7)	10	353,570.35
Northern Mindanao (Region 10)	11	38,760.77
Cordillera Administrative Region	13	44,501.99
Subtotal		*₱ 10,907,168.43*
Above the statutory minimum wage		
National Capital Region	3	12,213,730.57
Ilocos Region (Region 1)	5	493,597.47
Central Luzon (Region 3)	6	3,635,251.60
Calabarzon Growth Corridor Area (Region 4-A)	8	7,929,612.52
Davao Region (Region 11)	12	133,738.60
Subtotal		*₱ 24,405,930.76*
Total		**₱35,313,099.19**

[60] Exhibits "P-12", "P-13", and "P-18" to "P-21".
[61] Annex 1 of Exhibit "P-14".
[62] Annexes 2 to 13 of Exhibit "P-14".
[63] Exhibit "P-15".

As shown in *Annexes 2 to 13* of the ICPA's revised report, the gross pay includes the basic pay, COLA, incentive pay, rest day pay, night differential pay, overtime pay, and holiday pay. Holiday pay, overtime pay and night shift differential pay earned by MWE are exempt from withholding tax while 13th month pay and other benefits that do not exceed the ₱30,000.00 threshold are likewise exempt from withholding tax, as provided under RR No. 02-98, as amended by RR No. 10-2008, to wit:

> "Sec. 2.78.1. *Withholding of Income Tax on Compensation Income.* –
>
> xxx xxx xxx
>
> (B) *Exemptions from Withholding Tax on Compensation.* – xxx
>
> xxx xxx xxx
>
> (11) *Thirteenth (13th) month pay and other benefits.* –
>
> (a) **Thirteenth (13th) month pay** equivalent to the mandatory one (1) month basic salary of officials and employees of the government, (whether national or local), including government-owned or controlled corporations, and or private offices received after the twelfth (12th) month pay;
>
> (b) **Other benefits** such as Christmas bonus, productivity incentive bonus, loyalty award, gifts in cash or in kind and other benefits of similar nature actually received by officials and employees of both government and private offices. xxx
>
> The above stated exclusions (a) and (b) shall cover benefits paid or accrued during the year provided that the total amount shall **not exceed thirty thousand pesos (P30,000.00)** which may be increased through rules and regulations issued by the Secretary of Finance, upon recommendation of the Commissioner, after considering, among others, the effect on the same of the inflation rate at the end of the taxable year.
>
> xxx xxx xxx
>
> (13) Compensation income of MWEs who work in the private sector and being paid the Statutory Minimum Wage (SMW), as fixed by Regional Tripartite Wage and Productivity

> Board (RTWPB)/National Wages and Productivity Commission (NWPC), applicable to the place where he/she is assigned.
>
> xxx xxx xxx
>
> **Holiday pay, overtime pay, night shift differential pay and hazard pay earned by the aforementioned MWE shall likewise be covered by the above exemption.** Provided, however, that an employee who receives/ earns additional compensation such as commissions, honoraria, fringe benefits, benefits in excess of the allowable statutory amount of P30,000.00, taxable allowances and other taxable income other than the SMW, holiday pay, overtime pay, hazard pay and night shift differential pay shall not enjoy the privilege of being a MWE and, therefore, his/her entire earnings are not exempt from income tax and, consequently, from withholding tax." *(Emphasis supplied)*

Thus, the total amount of ₱10,907,168.43, as computed above, is exempt from withholding tax on compensation. Accordingly, the cost of services amounting only to ₱4,948,562.33, computed below, shall be disallowed as deduction for non-withholding of tax:

Cost of services per assessment	₱ 15,855,730.76
Cost of services – at or below SWM	10,907,168.43
Cost of services subject to withholding tax	**₱4,948,562.33**

b.2. Operating expenses (i.e., Ammunition and training, utilities and repair and maintenance)

Petitioner avers that the assessment did not establish whether the income payments made by petitioner under the foregoing items are subject to the expanded withholding tax (EWT). Unless duly notified in writing by respondent that petitioner is obligated to withhold on income payments to its local suppliers, the duty to withhold cannot be compelled.

Petitioner adds that to be subject to EWT, the income payment must be one of the items enumerated under Section 2.57.2 of RR No. 02-98, as amended. And a cursory examination of the items of income payments subject to EWT under the said regulation will show that the subject items are not among those which are subject to 1% or 2%. Thus, this portion of the present assessment must be cancelled and withdrawn.

We rule that this particular assessment should not be disturbed, in the absence of proof submitted by petitioner to the contrary.

Tax assessments by tax examiners are presumed correct 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.[64]

In this case, petitioner failed to prove that the subject items mentioned above are not among those that are subject to EWT under RR No. 02-98, as amended.

Therefore, the following expenses shall be disallowed as deductions from petitioner's gross income:

Cost of services	₱ 4,948,562.33
Ammunition and training	15,255.38
Utilities	82,736.95
Repair and maintenance	15,707.52
Total	**₱5,062,262.18**

In sum, petitioner is liable for basic deficiency income tax for taxable year 2009 in the amount of ₱1,577,522.93, computed as follows:

Taxable Net Income per ITR		₱ 1,266,967.95
Add: Adjustments		
50% Disallowed Operating Exp. - unsupported	₱ 196,147.59	
100% Disallowed Cost of Services & Operating Exp. – non-withholding	5,062,262.18	5,258,409.77
Adjusted Taxable Net Income		6,525,377.72
Income Tax Due		1,957,613.32
Less: Payments/tax credit		380,090.39
Deficiency Income Tax		**₱1,577,522.93**

[64] *Commissioner of Internal Revenue vs. Bank of the Philippine Islands*, G.R. No. 134062, April 17, 2007, citing *Sy Po v. Court of Appeals*, G.R. No. L-81446, August 18, 1988.

II. Improperly Accumulated Earnings Tax

Pursuant to Section 29 of the NIRC of 1997, as amended, in relation to RR No. 02-2001, respondent assessed petitioner for basic deficiency IAET arising from excessive accumulation of earnings over capital stock. The deficiency tax is computed as follows:[65]

Taxable income for the year	₱1,266,967.95
Less: Income tax paid	380,090.39
Net income after tax	886,877.56
Add: Retained earnings from previous year	4,375,885.16
Accumulated earnings as of December 31, 2009	5,262,762.72
Less: Amount that may be retained – capital stock	50,000.00
Earnings in excess of capital stock	5,212,762.72
Less: Appropriated retained earnings	-
Improperly accumulated earnings	5,212,762.72
Multiply by IAET rate	10%
Basic Deficiency Improperly Accumulated Earnings Tax Due	**₱521,276.27**

Petitioner claims that it is entitled to retain earnings for corporate expansion projects and/or programs requiring considerable capital expenditure. Likewise, respondent has allegedly failed to acknowledge the nature of petitioner's business as a security agency, which is required to keep a substantial amount of contingency funds.

Petitioner's contention is untenable.

Section 3 of RR No. 2-2001 provides as follows:

> "SECTION 3. *Determination of Reasonable Needs of the Business.* – An accumulation of earnings or profits (including undistributed earnings or profits of prior years) is unreasonable if it is not necessary for the purpose of the business, considering all the circumstances of the case. To determine the 'reasonable needs' of the business in order to justify an accumulation of earnings, these Regulations hereby adhere to the so-called 'Immediacy Test' under American jurisprudence as adopted in this jurisdiction. Accordingly, the term *'reasonable needs of the business'* are hereby construed to mean the immediate needs of the business, including reasonably anticipated needs. In either case, the corporation should be able to prove an immediate need for the accumulation of the earnings and profits, or the direct correlation of anticipated needs to such accumulation

[65] Exhibit "P-8", docket, vol. I, pp. 306 and 308.

of profits. Otherwise, such accumulation would be deemed to be not for the reasonable needs of the business, and the penalty tax would apply.

For purposes of these Regulations, the following constitute accumulation of earnings for the reasonable needs of the business:

a) Allowance for the increase in the accumulation of earnings up to 100% of the paid-up capital of the corporation as of Balance Sheet date, inclusive of accumulations taken from other years;

b) **Earnings reserved for definite corporate expansion projects or programs requiring considerable capital expenditure as approved by the Board of Directors or equivalent body**;

c) Earnings reserved for building, plants or equipment acquisition as approved by the Board of Directors or equivalent body;

d) Earnings reserved for compliance with any loan covenant or pre-existing obligation established under a legitimate business agreement;

e) Earnings required by law or applicable regulations to be retained by the corporation or in respect of which there is legal prohibition against its distribution;

f) In the case of subsidiaries of foreign corporations in the Philippines, all undistributed earnings intended or reserved for investments within the Philippines as can be proven by corporate records and/or relevant documentary evidence." *(Emphasis supplied)*

Based on the foregoing provision, the corporation should be able to prove an immediate need for the accumulation of the earnings and profits. And the Court finds that petitioner failed to prove the same.

Petitioner did not present any proof that its Board of Directors (or its equivalent body) indeed reserved the subject earnings for corporate expansion projects or programs. Petitioner could have submitted a board resolution, minutes of board meeting, and other documents that could support its claim. Basic is the rule that mere allegation is not evidence, and is not equivalent to proof. Thus, respondent's assessment must be sustained.

However, the Court noted that the formula used by respondent in computing for the deficiency IAET is not in accordance with Section 29 of the NIRC of 1997, as amended, which provides:

"SEC. 29. *Imposition of Improperly Accumulated Earnings Tax.* —

(A) *In General.* — In addition to other taxes imposed by this Title, there is hereby imposed for each taxable year on the improperly accumulated taxable income of each corporation described in Subsection B hereof, an improperly accumulated earnings tax equal to ten percent (10%) of the improperly accumulated taxable income.

xxx xxx xxx

(D) *Improperly Accumulated Taxable Income.* — For purposes of this Section, the term 'improperly accumulated taxable income' means taxable income adjusted by:

(1) Income exempt from tax;
(2) Income excluded from gross income;
(3) Income subject to final tax; and
(4) The amount of net operating loss carry-over deducted;

And reduced by the sum of:
(1) Dividends actually or constructively paid; and
(2) Income tax paid for the taxable year."

Applying the foregoing formula to the instant case, the deficiency IAET is recomputed as follows:

Taxable income for the year	₱1,266,967.95
Add:	
Income exempt from tax	-
Income excluded from gross income	-
Income subject to final tax	-
The amount of net operating loss carry-over deducted	-
Less:	
Dividends actually or constructively paid	-
Income tax paid for the taxable year	380,090.39
Improperly Accumulated Taxable Income	886,877.56
Multiply by IAET rate	10%
Basic Deficiency Improperly Accumulated Earnings Tax Due	**₱88,687.76**

WHEREFORE, premises considered, the instant Petition for Review is **PARTIALLY GRANTED**. Accordingly, the deficiency income tax and improperly accumulated earnings tax assessments for taxable year 2009 are **AFFIRMED** with **MODIFICATIONS** and petitioner is **ORDERED TO PAY** the modified amount of **₱2,082,763.36**, inclusive of the twenty-five percent (25%) surcharge imposed under Section 248(A)(3) of the NIRC of 1997, as amended, computed as follows:

Tax Type	Basic Tax	25% Surcharge	Total
Income Tax	₱ 1,577,522.93	₱ 394,380.73	₱ 1,971,903.66
Improperly Accumulated Earnings Tax	88,687.76	22,171.94	110,859.70
Total	**₱1,666,210.69**	**₱416,552.67**	**₱2,082,763.36**

In addition, petitioner is **ORDERED TO PAY**:

(a) Deficiency interest at the rate of twenty percent (20%) per annum on the basic deficiency income tax and improperly accumulated earnings tax computed from the dates indicated below until full payment thereof pursuant to Section 249(B) of the NIRC of 1997, as amended:

Tax Type	Basic Tax	Deficiency Interest Computed From
Income Tax	₱1,577,522.93	April 15, 2010
Improperly Accumulated Earnings Tax	₱ 88,687.76	January 15, 2011

(b) Delinquency interest at the rate of 20% per annum on the total amount of ₱2,082,763.36 and on the 20% deficiency interest which have accrued as afore-stated in (a), computed from September 25, 2013 until full payment thereof pursuant to Section 249(C) of the NIRC of 1997, as amended.

SO ORDERED.

AMELIA R. COTANGCO-MANALASTAS
Associate Justice

WE CONCUR:

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Associate Justice

CAESAR A. CASANOVA
Associate Justice

ATTESTATION

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

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Associate Justice
Chairperson

CERTIFICATION

Pursuant to Section 13, Article VIII 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