Republic of the Philippines
COURT OF TAX APPEALS
Quezon City

FIRST DIVISION

OAKWOOD OVERSEAS LIMITED,
Petitioner,

-versus-

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

CTA Case No. 8196
For: Assessment

Members:
DEL ROSARIO, PJ., Chairperson
UY, and
MINDARO-GRULLA, JJ.

Promulgated:
APR 29 2014, 12:20 p.m.

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DECISION

MINDARO-GRULLA, J.:

This resolves the Petition for Review filed on December 8, 2010 by Oakwood Overseas Limited as petitioner, against the Commissioner of Internal Revenue (CIR) as respondent, for the Court in Division, pursuant to Section 7 (a) (1) of Republic Act (RA) No. 1125, An Act Creating the Court of Tax Appeals, as amended[1], as well as Rule 4, Section 3 (a) (1), in relation to Rule 8, Section 4(a), of the Revised Rules of the Court of Tax Appeals (RRCTA)[2].

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1 Sec. 7. *Jurisdiction.* –The CTA shall exercise:

(a) Exclusive appellate jurisdiction to review by appeal, as herein provided:

x x x x x x

(1) Decisions of the Commissioner of Internal Revenue in cases involving disputed assessments, refunds or internal revenue taxes, fees or other charges, penalties in relation thereto, or other matters arising under the National Internal Revenue Code or other laws administered by the Bureau of Internal Revenue;

x x x x x x

2 Rule 4. Sec. 3. *Cases within the jurisdiction of the Court in Division.* – The Court in Division shall exercise:

Petitioner seeks the cancellation of the assessments issued against it for deficiency income tax, deficiency value-added tax (VAT), increments and compromise penalty in the aggregate amount of ₱1,154,125.61 for the fiscal year ended January 31, 2007.

Petitioner Oakwood Overseas Limited is a foreign corporation organized and existing under the laws of the British Virgin Islands duly licensed to do business in the Philippines, with address at the 30th Floor, Citibank Tower, 8741 Paseo de Roxas, Makati City.[3] It is engaged in the business of leasing condominium units.[4]

Respondent is the Commissioner of the Bureau of Internal Revenue (BIR) vested with authority to exercise the functions of said office, including, *inter alia*, the power to abate or cancel tax liability. She holds office at the BIR National Office Building, Agham Road, Diliman, Quezon City.

(a) Exclusive original over or appellate jurisdiction to review by appeal the following:

x x x x x x

(1) Decisions of the Commissioner of Internal Revenue in cases involving disputed assessments, refunds of internal revenue taxes, fees or other charges, penalties in relation thereto, or other matters arising under the National Internal Revenue Code or other laws administered by the Bureau of Internal Revenue;

x x x x x x

Rule 8. Sec. 4. *Where to appeal; mode of appeal.* –

(a) An Appeal from a decision or ruling or the inaction of the Commissioner of Internal Revenue on disputed assessments or claim for refund of internal revenue taxes erroneously or illegally collected; the decision or ruling of the Commissioner of Customs, the Secretary of Finance, the Secretary of Trade & Industry, the Secretary of Agriculture, and the Regional Trial Court in the exercise of their original jurisdiction, shall be taken to the Court by filing before it a petition for review as provided in Rule 42 of the Rules of Court. The Court in Division shall act on the appeal.

[3] Par. 1, Summary of Admitted Facts, Joint Stipulation of Facts and Issues (JSFI), Docket, p. 191.
[4] Par. 1, Stipulation of Facts, JSFI, Docket, p. 195.

On December 22, 2009, a Preliminary Assessment Notice[5] (PAN) was issued by respondent for alleged deficiency income tax and VAT for the fiscal year ended January 31, 2007. Petitioner protested the PAN on January 19, 2010.[6]

On January 20, 2010, respondent issued a Formal Assessment Notice (FAN), together with the corresponding Assessment Notices, assessing petitioner for deficiency income tax and VAT for the fiscal year ended January 31, 2007 and increments on late filing/payment of its Monthly VAT Declaration for March 2006.[7] On the same date, respondent also issued to petitioner a letter, together with the corresponding Assessment Notice, alleging that for the taxable year 2005, petitioner failed to file its Monthly Remittance Return of Creditable Income Tax and failed to register/keep books of accounts on time and suggesting the payment of compromise penalty of ₱33,400.00.[8] The FAN, the Assessment Notices for income tax, VAT and increments, and the letter dated January 20, 2010 regarding the compromise penalty with the corresponding Assessment Notice were all received by petitioner on January 21, 2010.[9]

Petitioner contested the assessments by way of a protest letter dated February 18, 2010, which was filed on February 19, 2010.[10]

In its protest letter dated January 14, 2010 against the PAN issued by respondent on December 22, 2009, petitioner already attached the documents necessary to support the defenses against the assessments. Hence, petitioner no longer attached the same supporting documents in its protest to the FAN.[11]

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[5] Exhibit "N".
[6] Exhibit "O".
[7] Par. 3, Summary of Admitted Facts, JSFI, Docket, pp. 191-192.
[8] Par. 4, Summary of Admitted Facts, JSFI, Docket, p. 192.
[9] Par. 5, Summary of Admitted Facts, JSFI, Docket, p. 192.
[10] Par. 6, Summary of Admitted Facts, JSFI, Docket, p. 192.
[11] Pars. 7 and 8, Summary of Admitted Facts, JSFI, Docket, p. 193.

Subsequently, respondent issued her Final Decision on Disputed Assessment (FDDA), a copy of which was received by petitioner on November 8, 2010.[12]

In the FDDA, respondent found petitioner liable for the following deficiency taxes:[13]

Income tax	₱ 891,670.83
Value-added tax	179,384.15
Increments on late filing of March 2006 Return	49,670.63
Compromise penalty	33,400.00
TOTAL	₱1,154,125.61

Aggrieved by the decision of respondent, petitioner filed its judicial appeal before this Court on December 8, 2010.

In an Answer[14] filed through registered mail on January 31, 2011, respondent interposed the following special and affirmative defenses:

> "4. She reiterates and repleads the preceding paragraphs of this answer as part of her Special and Affirmative Defenses;
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> 5. Section 228 of the Tax Code, partly provides:
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>> 'Sec. 228. Protesting of Assessment - 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

[12] Par. 9, Summary of Admitted Facts, JSFI, Docket, p. 193.
[13] Par. 10, Summary of Admitted Facts, JSFI, Docket, pp. 193-194.
[14] Docket, pp. 135-139.

> 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*.

Implementing the aforesaid provision, Section 3, 3.1.5 of Revenue Regulations No. 12-99 dated September 6, 1999, provides that the taxpayer shall submit the required documents in support of his protest within sixty (60) days from date of filing of his letter of protest, otherwise, the assessment shall become final, executory, and demandable. The phrase **'submit the required documents'** includes submission or presentation of the pertinent documents for scrutiny and evaluation by the Revenue Officer conducting the audit and the said Revenue Officer shall state this fact in his report of investigation.

In the instant case, pursuant to the report of re-investigation of the concerned BIR Examiner, the latter found that despite considerable length of time given to herein petitioner, it failed to submit the required documents in support of its protest against the BIR Formal Assessment Notice (FAN) dated 20 January 2010, within sixty (60) days from the filing of its administrative protest on February 19, 2010. Hence, the assessed deficiency income tax, value-added tax, increments on late filing/payment of VAT for March 2006 and compromise penalties of petitioner for Fiscal Year ending January 31, 2007 has already become final, executory and demandable. As such, this Honorable Court has no jurisdiction to act on the instant petition.

6. On the other hand, assuming without admitting that this Honorable Court has jurisdiction to act on the instant petition, Petitioner was assessed for deficiency income tax,

value-added tax, increments on late filing/payment of VAT for March 2006 and compromise penalties for Fiscal Year ending January 31, 2007, for the reason that during the administrative investigation of its tax case by the BIR, petitioner failed to substantiate or submit supporting evidence against the BIR findings, more specifically shown under the Details of Discrepancies attached to the Formal Assessment Notice (FAN) dated January 20, 2010, the Preliminary Assessment Notice (PAN) dated December 22, 2009, and Final Decision on Disputed Assessment dated October 28, 2010, which are briefly discussed hereunder, viz:

A.) On Deficiency Income Tax:

-Petitioner failed to substantiate or submit certain documents or evidence in support of its claimed deductions or expenses (i.e. Depreciation and amortization, condominium dues, taxes and licenses and miscellaneous) in violation of **Section 34 (A)(1)(b) of the 1997 Tax Code**, which states that: *'No deductions from gross income shall be allowed under Subsection (A) hereof, unless the taxpayer shall substantiate with sufficient evidence, such as official receipts or adequate records; (1) the amount of expense being deducted...'*

Hence, 50% of the said claimed expenses or a total of P4,041,789.50 were disallowed since the BIR has no means by which to ascertain the correctness and accuracy of the said claimed expenses of petitioner following the requirement under **Section 2.4 (c) of RMC 23-2000** which states that: *'If there is no 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 deduction that may be allowable in computing the taxpayer's taxable income, bearing heavily against the taxpayer whose inexactitude is of his own making...'*

-Petitioner failed to substantiate or submit evidence such as official receipts or equivalent adequate record in support of its claimed Share in Home Expenses per FS/ITR in the amount of P1,467,064.00. Hence, the same was disallowed pursuant to **Section 34 (A)(1)(b) of the 1997 Tax Code,** which states that: '*No deductions from gross income shall be allowed under Subsection (A) hereof, unless the taxpayer shall substantiate with sufficient evidence, such as official receipts or adequate records; (1) the amount of expense being deducted...'*

-Petitioner's claimed excess credit carried-over in the amount of P186,819.00 for fiscal year ending January 31, 2007 cannot be credited against its deficiency income tax since the said amount was already carried forward to the succeeding year, pursuant to **Section 2.58.3 of Revenue Regulations No. 2-98**.

B.) On Deficiency Value-Added Tax:

-Petitioner VAT payments for fiscal year ending January 31, 2007 amounts to P561,274.58 only, resulting to an under remittance of its VAT payable in the amount of P102,049.90. Hence, petitioner was assessed pursuant to Section 108 of the 1997 Tax Code.

-Petitioner belatedly filed its VAT return (BIR Form 2550M) for the month of March 2006 and failed to pay the tax due thereon on the date prescribed by law. Consequently, the corresponding penalties for late filing and payment thereof were imposed pursuant to Section 114(A) of the 1997 Tax Code in relation to Section 248(A) of the same Code.

C.) On Compromise Penalty:

-Petitioner failed to file its monthly remittance return of creditable income taxes withheld (expanded) in violation of Section 2.58(A) of Revenue Regulations No. 2-98. Hence, it was assessed a compromise penalty of P2,400.00, pursuant to Section 255 of the 1997 Tax Code.

-Petitioner belatedly filed and paid its VAT liability due for the month of March 2006 in violation of Section 4.114-1 of Revenue Regulations No. 16-2005. Hence, it was assessed a compromise penalty of P16,000.00, pursuant to Section 255 of the 1997 Tax Code.

-Petitioner failed to register/keep the required books of accounts in violation of Sections 232 and 235 of the 1997 Tax Code. Hence, it was assessed a compromise penalty of P15,000.00, pursuant to Section 255 of the 1997 Tax Code.

7. Respondent fully complied with the due process requirement mandated under Section 228 of the 1997 Tax Code, as implemented by Revenue Regulations No. 12-99, when the disputed Preliminary Assessment Notice (PAN) dated December 22, 2009 and Formal Assessment Notice (FAN) dated January 20, 2010 was issued to herein petitioner. Records clearly show that petitioner was duly afforded an opportunity to controvert the initial findings of the respondent involving its deficiency taxes for fiscal year ending January 31, 2007 through the issuance of a Notice for Informal Conference and Preliminary Assessment Notice (PAN) dated December 22, 2009. Likewise, petitioner was duly appraised by the respondent of the factual and legal basis on how and why he (respondent) arrived (at) such a deficiency income tax, value-added tax, increments on late filing/payment of VAT for March 2006 and compromise penalties for Fiscal Year ending January 31, 2007, through the issuance of the Details of Discrepancies attached to the Formal Assessment Notice (FAN) dated January 20, 2010, the Preliminary Assessment Notice (PAN) dated December 22, 2009 and Final Decision on Disputed Assessment dated October 28, 2010, as well as other BIR Correspondence to petitioner which are found in the BIR records of this case.

8. The assessments issued against petitioner for deficiency income tax, value-added tax, increments on late filing/payment of VAT for March 2006 and compromise penalties for Fiscal Year ending January 31, 2007 were made in accordance with law and regulations.

9. All presumptions are in favor of the correctness of tax assessments issued by the respondent."

The case was then set for pre-trial conference on March 11, 2011.[15] The Pre-Trial Brief for the Petitioner[16] was filed on March 8, 2011; while respondent's Pre-Trial Brief[17] was filed on April 6, 2011.

Thereafter, the parties filed their Joint Stipulation of Facts and Issues[18], through registered mail on May 13, 2011 and received by this Court on May 27, 2011, and their Supplemental Joint Stipulation of Facts and Issues[19] on June 2, 2011. In a Resolution[20] dated June 8, 2011, the Joint Stipulation of Facts and Issues and the Supplemental Joint Stipulation of Facts and Issues were approved and the pre-trial conference was considered terminated. Subsequently, a Pre-Trial Order was issued by this Court on July 4, 2011.[21] An Amended Pre-Trial Order was later issued on July 26, 2011.[22]

Petitioner presented Atty. Joseph Anthony M. Alejandro as witness. After completion of the presentation and the formal offer of the evidence for the petitioner, this Court admitted as evidence for petitioner Exhibits "A" to "W" as per this Court's Resolutions dated September 29, 2011,[23] January 04, 2012,[24] and March 28, 2012[25].

The documentary evidence formally offered and admitted are as follows:

Exhibits	Description
A	Secretary's Certificate dated June 2, 2011
B	Secretary's Certificate dated June 2, 2011
C	License to Transact Business in the Philippines issued by the Securities and

[15] Docket, p. 141.
[16] Docket, pp. 142-153.
[17] Docket, pp. 159-163.
[18] Docket, pp. 191-200.
[19] Docket, pp. 211-214.
[20] Docket, p. 216.
[21] Docket, pp. 228-246.
[22] Docket, pp. 483-501.
[23] Docket, pp. 735-736.
[24] Docket, pp. 772-777.
[25] Docket, pp. 790-791.

	Exchange Commission ("SEC") to OOL dated January 22, 1996
D	Tentative Income Tax Return for fiscal year ended January 31, 2007
D-1	Statement "FOR: Atty. Joseph Anthony M. Alejandro" and signature above the said statement
E	Final Income Tax Return for fiscal year ended January 31, 2007
E-1	Signature of Atty. Joseph Anthony M. Alejandro
E-2	Net Operating Loss for 2005 (₱1,873,192.00)
E-3	Net Operating Loss (Unapplied) for 2005 (₱1,873,192.00)
E-4	Net Operating Loss for 2006 (₱3,784,636.00)
E-5	Net Operating Loss (Unapplied) for 2006 (₱3,784,636.00)
E-6	Condominium dues and expenses for fiscal year ended January 31, 2007
E-7	Share in home office expenses for fiscal year ended January 31, 2007
F	Monthly Value-Added Tax Declaration for the month of February 2006
F-1-1	Signature above the statement "FOR: Atty. Joseph Anthony M. Alejandro"
F-1	Development Bank of the Philippines ("DBP") BIR Tax Payment deposit slip dated March 22, 2006
G	Quarterly Value-Added Tax Return for the period of January 2006 to March 2006
G-1-1	Signature above the statement "FOR: Atty. Joseph Anthony M. Alejandro"

G-1	DBP BIR Tax Payment deposit slip dated May 2, 2006
H	Monthly Value-Added Tax Declaration for the month of June 2006
H-1-1	Signature above the statement "FOR: Atty. Joseph Anthony M. Alejandro"
H-1	DBP BIR Tax Payment deposit slip dated July 20, 2006
I	Quarterly Value-Added Tax Return for the period of April 2006 to June 2006
I-1	Signature above the statement "FOR: Atty. Joseph Anthony M. Alejandro
J	Monthly Value-Added Tax Declaration for the month of July 2006
J-1	Signature above the statement "FOR: Atty. Joseph Anthony M. Alejandro"
K	Monthly Value-Added Tax Declaration for the month of August 2006
K-1-1	Signature above the statement "FOR: Atty. Joseph Anthony M. Alejandro"
K-1	DBP BIR Tax Payment deposit slip dated September 20, 2006
L	Quarterly Value-Added Tax Return for the period of July 2006 to September 2006
L-1-1	Signature above the statement "For: Atty. Joseph Anthony M. Alejandro"
L-1	DBP BIR Tax Payment deposit slip dated October 20, 2006
M	Monthly Value-Added Tax Declaration for the month of November 2006
M-1-1	Signature above the statement "For: Atty. Joseph Anthony M. Alejandro"
M-1	DBP BIR Tax Payment deposit slip dated December 22, 2006

N	Preliminary Assessment Notice dated December 22, 2009 ("PAN")
N-1	Letter of the BIR to OOL dated December 22, 2009
O	PAN Protest Letter dated January 14, 2010
O-1-1	Statement "FOR: J.A.M Alejandro" and signature above the said statement
O-1-2	Statement containing OOL's request for the BIR to inform it if additional documents are necessary
O-1-3	Schedule comparing the amounts and figures declared by OOL under "2007 Tentative FS" vis-à-vis the amounts and figures declared by OOL under "2007 Audited FS"
O-1-4	Schedule showing the reconciliation of the monthly gross receipts and VAT remittances of OOL in relation to the rental revenue of OOL as stated in its Audited Financial Statements
O-1	Tentative Financial Statements as of and for fiscal year ended January 31, 2007
O-1-a	Statement of Revenues and Expenses as of and for the fiscal year ended January 31, 2007 of the Tentative Financial Statements of OOL for the fiscal year ended January 31, 2007
O-1-a-1	Rental revenue as for fiscal year ended January 31, 2007 (₱5,527,704.00)
O-2	Audited Financial Statements as of and for fiscal year ended January 31, 2007
O-2-a	Net Operating Loss for 2005 (₱1,873,192.00)
O-2-b	Net Operating Loss (Balance) for 2005 (₱1,873,192.00)

O-2-c	Net Operating Loss for 2006 (₱4,737,174.00)
O-2-d	Net Operating Loss (Balance) for 2006 (₱4,737.174.00)
O-2-e	Statement of Revenues and Expenses as of and for the fiscal year ended January 31, 2007 of the Audited Financial Statements of OOL for the fiscal year ended January 31, 2007
O-2-e-1	Condominium dues and expenses for fiscal year ended January 31, 2006
O-2-e-2	Condominium dues and expenses for fiscal year ended January 31, 2007
O-2-e-3	Share in home office expenses for fiscal year ended January 31, 2007
O-2-e-4	Rental revenue as for fiscal year ended January 31, 2007 (₱4,677,288.00)
O-2-f	Schedule providing for the cost, accumulated depreciation, depreciation for the year, and net book values for the years 2006 and 2007 (Note 4 (Office Condominium units))
O-2-g	Schedule on the useful life of the condominium units of OOL (twenty-five (25) years)
O-3	Summary of condominium dues of OOL for fiscal year ended January 31, 2007
O-3-a	Pacific Star Building Condominium Corporation Billing Statement No. 177505
O-3-b	Pacific Star Building Condominium Corporation Billing Statement No.177797
O-3-c	Pacific Star Building Condominium Corporation Billing Statement No. 178195
O-3-d	Pacific Star Building Condominium Corporation Billing Statement No. 178475

O-3-e	Pacific Star Building Condominium Corporation Billing Statement No. 179031
O-3-f	Pacific Star Building Condominium Corporation Billing Statement No. 179288
O-3-g	Pacific Star Building Condominium Corporation Billing Statement No. 179598
O-3-h	Pacific Star Building Condominium Corporation Billing Statement No. 179944
O-3-i	Pacific Star Building Condominium Corporation Billing Statement No. 180300
O-3-j	Pacific Star Building Condominium Corporation Billing Statement No. 180588
O-3-k	Pacific Star Building Condominium Corporation Billing Statement No. 180987
O-3-l	Pacific Star Building Condominium Corporation Billing Statement No. 181395
O-4	Summary of Taxes and Licenses of OOL for fiscal year ended January 31, 2007
O-4-a	OOL's Community Tax Certificate No. 163858
O-4-b	Official Receipt No. 7797677 for OOL's business registration
O-4-c	Barangay Clearance
O-4-d	Commonwealth Insurance Company's Official Receipt No. 877952
O-4-e	Commonwealth Insurance Company's Declarations for Policy No. CGL 69452
O-4-f	Petty Cash voucher issued by Romulo Mabanta Buenaventura Sayoc & delos Angeles
O-4-g	Real Property Tax Receipt No. MKT 0388408
O-4-h	Pacific Star Building Condominium Corporation Billing Statement No. 178195

P	Formal Assessment Notice dated January 20, 2010 ("FAN")
P-1	Letter of the BIR to OOL dated January 20, 2010
P-2	Assessment Notice dated January 20, 2010 for Income Tax
P-3	Assessment Notice dated January 20, 2010 for Value-Added Tax
P-4	Assessment Notice dated January 20, 2010 for Value-AddedTax Increments
P-5	Assessment Notice dated January 20, 2010 for Compromise Penalty
Q	FAN Protest Letter dated February 18, 2010
Q-1	Statement "FOR: J.A.M. Alejandro" and signature above the said statement
Q-2	Statement containing OOL's request for the BIR to inform it if additional documents are necessary
Q-3	Schedule comparing the amounts and figures declared by OOL under "2007 Tentative FS" vis-à-vis the amounts and figures declared by OOL under " 2007 Audited FS"
Q-4	Schedule showing the reconciliation of the monthly gross receipts and VAT remittances of OOL in relation to the rental revenue of OOL as stated in its Audited Financial Statements
R	Annual Income Tax Return for fiscal year ended January 31, 2005
R-1-1	Net Operating Loss for 2005 (₱1,873,192.00)
R-1-2	Net Operating Loss (Unapplied) for 2005 (₱1,873,192.00)
R-1-3	Signature of Atty. Joseph Anthony M. Alejandro

R-1	Audited Financial Statements as of and for fiscal year ended January 31, 2005
R-1-a	Net Operating Loss for 2005 (₱1,873,192.00)
R-1-b	Net Operating Loss (Balance) for 2005 (₱1,873,192.00)
S	Annual Income Tax Return for fiscal year ended January 31, 2006
S-1-1	Net Operating Loss for 2005 (P1,873,192.00)
S-1-2	Net Operating Loss (Unapplied) for 2005 (₱1,873,192.00)
S-1-3	Net Operating Loss for 2006 (₱4,737,174.00)
S-1-4	Net Operating Loss (Unapplied) for 2006 (₱4,737,174.00)
S-1-5	Signature of Atty. Joseph Anthony M. Alejandro
S-1	Audited Financial Statements as of and for fiscal year ended January 31, 2006
S-1-a	Net Operating Loss for 2005 (₱1,873,192.00)
S-1-b	Net Operating Loss (Balance) for 2005 (₱1,873,192.00)
S-1-c	Net Operating Loss for 2006 (₱4,737,174.00)
S-1-d	Net Operating Loss (Balance) for 2006 (₱4,737,174.00)
T	Annual Income Tax Return for fiscal year ended January 31, 2008
T-1-1	Net Operating Loss for 2005 (₱1,873,192.00)

T-1-2	Net Operating Loss (Unapplied) for 2005 (₱1,873,192.00)
T-1-3	Net Operating Loss for 2006 (₱3,784,636.00)
T-1-4	Net Operating Loss (Unapplied) for 2006 (₱3,784,636.00)
T-1-5	Signature of Atty. Joseph Anthony M. Alejandro
T-1	Audited Financial Statements as of and for fiscal year ended January 31, 2008
T-1-a	Net Operating Loss for 2006 (₱4,737,174.00)
T-1-b	Net Operating Loss (Balance) for 2006 (₱4,737,174.00)
U	Annual Income Tax Return for fiscal year ended January 31, 2009
U-1-1	Net Operating Loss for 2006 (₱3,784,636.00)
U-1-2	Net Operating Loss (Unapplied) for 2006 (₱3,784,636.00)
U-1-3	Statement "FOR: Atty. Joseph Anthony M. Alejandro" and signature above the said statement
U-1	Audited Financial Statements as of and for fiscal year ended January 31, 2009
V	Final Decision on the Disputed Assessment dated October 28, 2010 ("Final Decision")
W	Judicial Affidavit in Lieu of Direct Examinations of Joseph Anthony M. Alejandro
W-1	Signature of Joseph Anthony M. Alejandro

Respondent thru counsel presented Ofelia L. Metrillo and Ruby S. Munion, as witnesses. Respondent formally offered Exhibits "1" to "22",[26] which were admitted in the Resolution[27] dated January 25, 2013, with the exception of Exhibit "9-A"; which was denied admission for respondent's failure to have the same identified in court and considering that the description mentioned in respondent's Formal Offer of Evidence does not correspond to the duly marked exhibit.

Respondent's documentary exhibits are as follows:

Exhibit	Description
1	BIR Records bearing the internal revenue tax liabilities of petitioner for Fiscal Year ending January 31, 2007, that is, covering the period February 1, 2006 to January 31, 2007
2	Tax Verification Notice (TVN) No. 00050797 dated Sept. 24, 2007 of the BIR
2-A	Name and specimen signature of Roberto A. Baquiran, Revenue District Officer, BIR RDO 50-South Makati
2-B	Date of Receipt of petitioner of the said Tax Verification Notice (TVN) No. 00050797 dated Sept. 24, 2007
3	BIR List of Requirements/Documents per RMO 53-98 to be submitted by petitioner
3-A	Name and specimen signature of Ofelia L. Metrillo, Revenue Officer
3-B	Date of Receipt of petitioner of the said BIR List of Requirements per RMO 53-98
4	Second Request for Presentation of Records dated October 11, 2007 of the BIR
4-A	Name and specimen signature of Medina C. Lopez, Group Supervisor

[26] Docket, pp. 875-888.
[27] Docket, pp. 908-909.

4-B	Date of Receipt of petitioner of the said Second Request for Presentation of Records dated October 11, 2007 of the BIR
5	Final Notice dated January 7, 2008 of the BIR
5-A	Name and specimen signature of Salvador V.R. Lasala, Asst. Revenue District Officer, RDO 50 South Makati
5-B	Date of Receipt of petitioner of the said Final Notice dated January 7, 2008 of the BIR
6	Memorandum Report dated January 30, 2008 of RO Ofelia L. Metrillo
6-A	Memorandum Report dated January 30, 2008 of RO Ofelia L. Metrillo
7	Subpoena Duces Tecum dated February 7, 2008 issued by the Regional Director, BIR RR8 Makati City to petitioner
8	BIR Letter-Complaint dated November 5, 2008, duly signed by the Regional Director, BIR RR8 Makati City
8-A	Date of Filing of the BIR of the said Letter-Complaint dated Nov. 5, 2008
8-B	Name and specimen signature of Ma. Nieva A. Guerrero, OIC-Regional Director, BIR RR8 Makati City
9	Sworn Affidavit dated Nov. 5, 2008, duly signed by Ofelia L. Metrillo, Revenue Officer
10	Referral Memorandum dated January 19, 2009
10-A	Name and specimen signature of Rhodora G. Icaranom, Asst. Revenue District Officer, BIR RDO 50-South Makati
11	Letter dated January 22, 2009 of the BIR
11-A	Name and specimen signature of Roberto A. Baquiran, Revenue District Officer of BIR RDO 50 South Makati

11-B	Date of receipt of petitioner of the said Letter dated January 22, 2009 of the BIR
12	Memorandum Report dated April 20, 2009 of RO Ofelia L. Metrillo
12-A	Name and specimen signature of RO Ofelia L. Metrillo
13	BIR Preliminary Assessment Notice (PAN) dated December 22, 2009
13-A	Name and specimen signature of Alfredo V. Misajon, Regional Director, BIR RR8 Makati City
13-B	Details of Discrepancies attached to the said BIR Preliminary Assessment Notice (PAN) dated December 22, 2009
13-C	Name and specimen signature of Alfredo V. Misajon, Regional Director, BIR RR8 Makati City
13-D	Letter dated December 22, 2009 of the BIR attached to the said Preliminary Assessment Notice (PAN) dated December 22, 2009
13-E	Date of receipt of petitioner of the said Preliminary Assessment Notice (PAN) dated December 22, 2009 with attached Letter dated December 22, 2009 and Details of Discrepancies
14	BIR Formal Assessment Notice (FAN) and Letter of Demand dated January 20, 2010
14-A	Name and specimen signature of Jaime B. Santiago, CESO V, Regional Director, BIR RR8 Makati City
14-B	Details of Discrepancies attached to the said BIR Formal Assessment Notice (FAN) and Letter of Demand dated January 20, 2010
14-C	Name and specimen signature of Jaime B. Santiago, CESO V, Regional Director, BIR RR8 Makati City

14-D	Letter dated January 20, 2010 of the BIR attached to the said Formal Assessment Notice (FAN) and Letter of Demand dated January 20, 2010
14-E	Date of receipt of petitioner of the said BIR Formal Assessment Notice (FAN) and Letter of Demand dated January 20, 2010 with attached Letter dated January 20, 2010 and Details of Discrepancies
15	Tax Verification Notice (TVN) No. 00149081 dated March 22, 2010 of the BIR
15-A	Name and specimen signature of Ricardo B. Espiritu, Revenue District Officer of BIR RDO 50 South Makati
15-B	Date of Receipt of petitioner of the said Tax Verification Notice (TVN) No. 00149081 dated March 22, 2010
16	BIR Letter dated September 3, 2010
16-A	Name and specimen signature of Ricardo B. Espiritu, Revenue District Officer of BIR RDO 50 South Makati
16-B	Date of Receipt of petitioner of the said BIR Letter dated September 3, 2010
17	Memorandum Report dated September 15, 2010 of Revenue Officer Ruby S. Munion
17-A	Name and specimen signature of Revenue Officer Ruby S. Munion
18	Final Decision on Disputed Assessment (FDDA) dated October 28, 2010 of the BIR Regional Director, RR8 Makati City
18-A	Name and specimen signature of Jaime B. Santiago, CESO V, Regional Director, BIR RR8 Makati City
18-B	Details of Discrepancies dated October 28, 2010 attached to the said Final Decision on Disputed Assessment (FDDA) dated October 28, 2010

18-C	Name and specimen signature of Jaime B. Santiago, CESO V, Regional Director, BIR RR8 Makati City
18-D	Date of Receipt of petitioner of the said BIR Final Decision on Disputed Assessment (FDDA) dated October 28, 2010 with attached Details of Discrepancies dated October 28, 2010
19	Preliminary Collection Letter dated March 28, 2011 of the BIR
19-A	Name and specimen signature of Ricardo B. Espiritu, Revenue District Officer of BIR RDO 50 South Makati
20	Final Notice Before Seizure dated April 25, 2011 of the BIR
20-A	Name and specimen signature of Ricardo B. Espiritu, Revenue District Officer of BIR RDO 50 South Makati
21	Judicial Affidavit dated April 20, 2012 of Revenue Officer Ofelia L. Metrillo
21-A	Name and specimen signature of Revenue Officer Ofelia L. Metrillo
22	Judicial Affidavit dated July 2, 2012 of Revenue Officer Ruby S. Munion
22-A	Name and specimen signature of Revenue Officer Ruby S. Munion

Petitioner submitted its Memorandum[28] on June 3, 2013; while respondent filed her Manifestation and Motion (Memorandum for Respondent)[29] through registered mail on June 3, 2013, manifesting, among others, that she is adopting the special and affirmative defenses in her Answer dated January 28, 2011. Accordingly, the case was submitted for decision on June 20 2013.[30]

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[28] Docket, pp. 933-961.
[29] Docket, pp. 963-968.
[30] Resolution dated June 20, 2013, Docket, pp. 971-972.

The parties submitted the following issues[31] for this Court's disposition:

"1. Whether or not Petitioner complied with Section 228 of the National Internal Revenue Code, as implemented by Section 3 of Revenue Regulations No. 12-99 (dated September 6, 1999), which requires the taxpayer to submit relevant supporting documents within sixty (60) days from the filing of the protest.

2. Whether or not Respondent specifically required Petitioner to submit additional documents in support of its contentions against the assessments for deficiency income tax, deficiency value-added tax, increments on late filing/payment of VAT for March 2006 and compromise penalties for fiscal year ended January 31, 2007.

3. Whether or not Petitioner is liable for the assessed deficiency income tax for fiscal year ended January 31, 2007 based on its failure to substantiate its claimed deductions or expenses on Depreciation and Amortization Expenses, Condominium Dues and Expenses, Taxes and License Expenses, and Miscellaneous Expenses in the total amount of ₱8,083,579.00 and Share in Home Office Expenses in the amount of ₱1,467,064.00.

4. Assuming the disallowance of the expenses is proper, whether or not the Net Operating Loss Carry-Over of Petitioner for the years 2005 and 2006 in the amount ₱1,873,192.00 and ₱3,784,636.00, respectively, may be applied against the taxable income of Petitioner for taxable fiscal year ended January 31, 2007.

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[31] Docket, pp. 197-199.

5. Whether or not petitioner is liable for the assessed deficiency value-added tax for fiscal year ended January 31, 2007 in the amount of ₱102,049.90.

6. Whether or not Petitioner is liable for increments due to the late filing and payment of VAT due for March 2006 consisting of 25% surcharge and 20% interest in the amount of ₱25,512.48 and ₱335.51, respectively.

7. Whether or not Petitioner is liable for compromise penalties on: (i) non-filing of monthly remittance return of creditable income taxes withheld (expanded), (ii) late filing and payment of VAT due for March 2006, and (iii) failure to register/keep books of accounts for fiscal year ended January 31, 2007.

8. Whether or not petitioner is liable for the assessments for deficiency income tax, deficiency value-added tax, increments on late filing/payment of VAT for March 2006 and compromise penalties for fiscal year ending January 31, 2007, in the total aggregate amount of **₱1,154,125.61**, inclusive of increments."

Anent the first and second stipulated issues concerning the submission of relevant supporting documents, petitioner alleged that it was able to submit supporting documents in compliance with Section 228 of the National Internal Revenue Code (NIRC) of 1997. According to petitioner, it submitted all the documents it believed were necessary to support its defenses when it filed its protest to the PAN. Despite petitioner's submissions, respondent ignored the protest and the attached supporting documents and issued the FAN, which is exactly the same as the PAN, on January

20, 2010. In both the PAN protest and the FAN protest, petitioner expressly requested that it be advised by respondent if additional documents must be submitted. However, after petitioner filed both the PAN protest and the FAN protest, respondent never required petitioner to submit specific additional supporting documents. Thus, petitioner believed that it was grossly unfair, if not malicious, for respondent to ignore the protests and supporting documents submitted by petitioner and then to declare in the Final Decision on Disputed Assessment that petitioner failed to submit supporting documents in accordance with Section 228 of the NIRC of 1997.

In the case of *Commissioner of Internal Revenue vs. First Express Pawnshop Company, Inc.*[32], the Supreme Court said that the term "relevant supporting documents" should be understood as 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. The BIR 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.

Records show that in both the protests to the PAN and the FAN, petitioner mentioned that a copy of the Final or the 2007 Audited Statements of Revenues and Expenses or Financial Statements that was filed on April 22, 2008 is attached to the protest and that it likewise attached to the protest a Summary of Taxes and Licenses and Condominium Dues. Furthermore, there is nothing in the records which would indicate that respondent required additional documents necessary to support petitioner's protest to the PAN. Since it was petitioner that will determine the documents necessary to support the legal basis in disputing a tax assessment, the documents submitted by petitioner together with the protest to the PAN, which are the very same documents mentioned in petitioner's protest to the FAN, are deemed to be the relevant supporting documents

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

as defined under Section 228 of the NIRC of 1997. Thus, respondent's allegation that the lapse of the sixty (60)-day period to submit supporting documents made the FAN final and executory deserves scant consideration.

Notably, in the Details of Discrepancies attached to the FDDA, it was mentioned that in the absence of accounting records or other documents necessary for the proper determination of the taxpayer's internal revenue tax liability, Section 6(B) of the NIRC of 1997, as amended, requires that the assessment of the tax be determined based on the Best Evidence Obtainable. Section 6(B) of the NIRC of 1997 reads:

> "SEC. 6. *Power of the Commissioner to Make Assessments and Prescribe Additional Requirements for Tax Administration and Enforcement*. -
>
> xxx xxx 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." *(Emphasis supplied)*

The power of the Commissioner to issue an assessment based on the best evidence obtainable was elaborated in the case of *Commissioner of Internal Revenue vs. Hantex Trading Co. Inc.*[33], wherein the Highest Tribunal ruled as follows:

> "The law allows the BIR access to all relevant or material records and data in the person of the taxpayer. It places no limit or condition on the type or form of the medium by which the record subject to the order of the BIR is kept. The purpose of the law is to enable the BIR to get at the taxpayer's records in whatever form they may be kept. Such records include computer tapes of the said records prepared by the taxpayer in the course of business. In this era of developing information-storage technology, there is no valid reason to immunize companies with computer-based, record-keeping capabilities from BIR scrutiny. *The standard is not the form of the record but where it might shed light on the accuracy of the taxpayer's return*.
>
> In *Campbell, Jr. v. Guetersloh*, the United States (U.S.) Court of Appeals (5th Circuit) declared that it is the duty of the Commissioner of Internal Revenue to investigate any circumstance which led him to believe that the taxpayer had taxable income larger than reported. Necessarily, this inquiry would have to be outside of the books because they supported the return as filed. He may take the sworn testimony of the taxpayer; he may take the testimony of third parties; he may examine and subpoena, if necessary, traders' and brokers' accounts and books and the taxpayer's book accounts. The Commissioner is not bound to

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

follow any set of patterns. The existence of unreported income may be shown by any practicable proof that is available in the circumstances of the particular situation. Citing its ruling in *Kenney v. Commissioner*, the U.S. appellate court declared that where the records of the taxpayer are manifestly inaccurate and incomplete, the Commissioner may look to other sources of information to establish income made by the taxpayer during the years in question.

xxx xxx xxx

The rule is that in the absence of the accounting records of a taxpayer, his tax liability may be determined by estimation. The petitioner is not required to compute such tax liabilities with mathematical exactness. Approximation in the calculation of the taxes due is justified. To hold otherwise would be tantamount to holding that skillful concealment is an invincible barrier to proof. **However, the rule does not apply where the estimation is arrived at arbitrarily and capriciously**.

We agree with the contention of the petitioner that, as a general rule, tax assessments by tax examiners are presumed correct and made in good faith. All presumptions are in favor of the correctness of a tax assessment. It is to be presumed, however, that such assessment was based on sufficient evidence. Upon the introduction of the assessment in evidence, a *prima facie* case of liability on the part of the taxpayer is made. If a taxpayer files a petition for review in the CTA and assails the assessment, the *prima facie* presumption is that the assessment made by the BIR is correct, and that in preparing the same, the BIR personnel regularly performed their duties. This rule for tax initiated suits is premised on several factors other than the normal evidentiary rule imposing proof obligation on the petitioner-taxpayer: the presumption of administrative regularity; the likelihood that the taxpayer will have access to the relevant information; and the desirability of bolstering the record-keeping requirements of the NIRC.

However, the *prima facie* correctness of a tax assessment does not apply upon proof that an assessment is utterly without foundation, meaning it is arbitrary and capricious. Where the BIR has come out with a 'naked assessment,' *i.e.*, without any foundation character, the determination of the tax due is without rational basis. In such a situation, the U.S. Court of Appeals ruled that the determination of the Commissioner contained in a deficiency notice disappears. *Hence, the determination by the CTA must rest on all the evidence introduced and its ultimate determination must find support in credible evidence.* " *(Emphasis supplied)*

Simply put, while respondent has the power to assess petitioner based on the best evidence obtainable and may resort to approximation in the calculation of the taxes due, the same should not be arrived at arbitrarily and capriciously.

In this case, the FDDA mentioned that petitioner failed to submit the required documents relative to its protest despite the considerable length of time given to it. Contrary to respondent's allegations, it must be noted that petitioner attached supporting documents in its protest to the PAN which were the same documents mentioned in petitioner's protest to the FAN. Also, a perusal of the BIR Records would show that the supporting documents such as a copy of the Final or the 2007 Audited Statements of Revenues and Expenses or Financial Statements, and a copy of the Summary of Taxes and Licenses and Condominium Dues were submitted to the BIR.[34] Clearly, petitioner timely submitted documents it deemed relevant to support its protests to the PAN and the FAN.

The Court will now proceed to determine the propriety of each of the assessed deficiency taxes.

I. DEFICIENCY INCOME TAX – ₱891,670.83

As stated in the Final Decision on Disputed Assessment, the deficiency income tax was computed as follows:[35]

Taxable Income (Loss) per Return		(₱4,022,939.00)
Add: Adjustments/Disallowances per investigation		
a. Disallowed Expenses (Schedule 1)	₱4,041,789.50	
b. Unsupported Share in Home Office Expenses	1,467,064.00	5,508,853.50
Taxable Income (Loss) per Audit		₱ 1,485,914.50
Tax Due thereon		₱ 520,070.08
Less: Tax Credits/Payments		
Prior Years Excess Credit	₱ 186,819.00	
Less: Excess Carried Over to Succeeding Year	186,819.00	-
Basic Tax Due		₱ 520,070.08
Add: Interest (05.16.07 to 12.10.10)		371,600.75
TOTAL AMOUNT DUE		**₱ 891,670.83**

A. Disallowance of 50% of Expenses - ₱4,041,789.50

Based on the purported failure of petitioner to provide documents or evidence to support its claimed deductions, respondent disallowed fifty percent (50%) of the following expenses claimed by petitioner:[36] ℒ

[34] Exhibit "1".
[35] Exhibit "V"; Par. 11, Summary of Admitted Facts, JSFI, Docket, p. 194.
[36] Par. 4, Stipulation of Facts, JSFI, Docket, p. 196.

DISALLOWED EXPENSES	
OPERATING EXPENSES PER FS	**AMOUNT**
Depreciation and Amortization	₱ 6,028,384.00
Condominium Dues and Expenses	1,652,451.00
Taxes and Licenses	402,117.00
Miscellaneous	627.00
Total	₱ 8,083,579.00
	50%
Disallowed Expenses	**₱4,041,789.50**

A.1. Depreciation Expense – ₱6,028,384.00

In its Petition[37], petitioner argued that its annual depreciation expense of ₱6,028,384.00 has been consistently claimed as deduction from gross income since 1997 in accordance with Section 34(F) of the NIRC of 1997, which provides:

> "SEC. 34. *Deductions from Gross Income*. – xxx
>
> xxx xxx xxx
>
> (F) *Depreciation*. –
>
> (1) *General Rule*. - There shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear (including reasonable allowance for obsolescence) of property used in the trade or business. xxx
>
> (2) *Use of Certain Methods and Rates*. - The term 'reasonable allowance' as used in the preceding paragraph shall include, but not limited to, an allowance computed in accordance with rules and regulations prescribed by the

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[37] Par. 23, Petition, Docket, p. 7.

Secretary of Finance, upon recommendation of the Commissioner, under any of the following methods:

(a) The straight-line method;"

The Court agrees with petitioner.

Based on the Supreme Court ruling in *Gutierrez vs. Collector (now Commissioner) of Internal Revenue*[38], a taxpayer may deduct from gross income a reasonable allowance for deterioration of property arising out of its use or employment in business or trade. Records indicate that petitioner is engaged in the business of leasing out condominium units.[39] There is no proof that the condominium units are being used for purposes other than for petitioner's business. As such, the related depreciation expense would be a valid ordinary business expense.

Moreover, as reflected in the Notes to Financial Statements as of and for the Year Ended January 31, 2007[40], the depreciation expense was computed using the generally accepted straight line depreciation method by dividing the total Condominium Units cost of ₱150,650,880.00[41] by its estimated useful life of twenty-five years[42]. This will yield an annual depreciation expense of ₱6,026,035.20, which is substantially the same amount as was charged. Hence, the disallowance made by respondent is improper.

A.2. Condominium Dues and Expenses – ₱1,652,451.00

[38] G.R. No. L-19537, May 20, 1965.
[39] Par. 1, Stipulation of Facts, JSFI, Docket, p. 195.
[40] Exhibit "O-2", Docket, p. 604.
[41] Exhibit "O-2-f", Docket, p. 617.
[42] Exhibit "O-2-g", Docket, p. 612.

Petitioner argued that respondent erred in disallowing the Condominium Dues and Expenses as these were not even claimed as deduction by petitioner.

Petitioner maintained that respondent overlooked the fact that petitioner did not claim Condominium Dues and Expenses as one of its deductible expenses; rather, as reflected in the Statements of Revenue and Expenses of the Audited Financial Statements attached to the Final Annual Income Tax Return, the Condominium Dues and Expenses of ₱1,652,451.00[43] pertained to fiscal year ended January 31, 2006.

Furthermore, petitioner's tax representative, Mr. Joseph Anthony M. Alejandro, stated the following in his Judicial Affidavit in Lieu of Direct Examination[44]:

> "40. Q: Why were the condominium dues and expenses not claimed as expense in the Final ITR?
>
> A: There was a pending legal issue between OOL and the Condominium Corporation regarding the titling of the area covered by their agreement. Accordingly, OOL did not recognize the Condominium Corporation's authority to bill OOL for condominium dues and expenses for fiscal year ended January 31, 2007.
>
> The fact that OOL did not incur condominium dues and expenses for fiscal year ended January 31, 2007 but only for fiscal year ended January 31, 2006 is reflected in the corresponding entries in the Statement of Revenues and Expenses of the Audited Financial Statements of OOL for fiscal year ended January 31, 2007, which have been

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[43] Exhibit "O-2-e-1" Docket, p. 608.
[44] Exhibit "W", Docket, p. 535.

previously marked as Exhibits 'O-2-e-1' and 'O-2-e-2', respectively."

Petitioner likewise submitted a Summary of Condominium Dues[45] and Billing Statements issued by Pacific Star Building Condominium Corporation for the year ended January 31, 2007 to controvert the allegations of respondent that the said expenses were not duly substantiated, the details of which are as follows:

DATE	BILLING NO.	CONDOMINIUM DUES
Feb-06	177505	₱ 143,906.00[46]
Mar-06	177797	143,906.00[47]
Apr-06	178195	143,906.00[48]
May-06	178475	143,906.00[49]
Jun-06	179031	71,953.00[50]
Jul-06	179288	158,296.60[51]
Aug-06	179598	158,296.60[52]
Sep-06	179944	158,296.60[53]
Oct-06	180300	158,296.60[54]
Nov-06	180588	158,296.60[55]
Dec-06	180987	158,296.60[56]
Jan-07	181395	158,296.60[57]
Total		₱ 1,755,653.20
Less: Adjustments		103,202.20
Balance, 31-Jan-07		**₱1,652,451.00**

As contended by petitioner, its Tentative Annual Income Tax Return for said period disclosed Direct Charges - Condo Dues amounting to ₱1,652,451.00[58], which was the basis of respondent in computing said disallowance included

[45] Exhibit "O-3", Docket, p. 619.
[46] Exhibit "O-3-a", Docket, p. 620.
[47] Exhibit "O-3-b", Docket, p. 621.
[48] Exhibit "O-3-c", Docket, p. 622.
[49] Exhibit "O-3-d", Docket, p. 623.
[50] Exhibit "O-3-e", Docket, p. 624.
[51] Exhibit "O-3-f", Docket, p. 625.
[52] Exhibit "O-3-g", Docket, p. 626.
[53] Exhibit "O-3-h", Docket, p. 627.
[54] Exhibit "O-3-i", Docket, p. 628.
[55] Exhibit "O-3-j", Docket, p. 629.
[56] Exhibit "O-3-k", Docket, p. 630.
[57] Exhibit "O-3-l", Docket, p. 631.
[58] Exhibit "D", Schedule 3, Docket, p. 544.

in the FDDA[59] dated October 28, 2010. On the other hand, petitioner's Final Annual Income Tax Return for the same period showed that petitioner declared nil[60] in Item 49 Direct Charges – Condo Dues. Respondent failed to consider the adjusted amount of Condominium Dues and Expenses declared by petitioner in its Final Financial Statements and Final Income Tax Return for the fiscal year ended January 31, 2007. Therefore, respondent has no basis in disallowing such expense which is in fact inexistent.

A.3. Taxes and Licenses and Miscellaneous Expenses – ₱402,117.00

Petitioner asserted that the taxes and licenses it claimed represent real property taxes and licenses, which are deductible from gross income under Section 34(C)(1) of the NIRC of 1997; while the miscellaneous expenses are ordinary and necessary business expenses deductible under Section 34(A)(1) of the NIRC of 1997. For easy reference, the said Tax Code provisions are quoted hereunder:

> "SEC. 34. *Deductions from Gross Income*. – xxx
>
> *(A) Expenses. –*
>
> (1) *Ordinary and Necessary Trade, Business or Professional Expenses*. -
>
> (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:

[59] Exhibit "V", Docket, p. 727.
[60] Exhibit "E-7", Docket, p. 549.

xxx xxx xxx

(C) *Taxes.* -

(1) *In General.* - Taxes paid or incurred within the taxable year in connection with the taxpayer's profession, trade or business, shall be allowed as deduction, xxx"

The Court finds petitioner's submission meritorious.

It may be observed that respondent based the amount of disallowed expenses for taxes and miscellaneous charges on petitioner's Tentative Annual ITR[61] and Tentative FS[62] for the fiscal year ended January 31, 2007, instead of the amount reflected in the Final Annual ITR. Contrary to respondent's contention of non-substantiation, petitioner was able to submit its Summary of Taxes and Licenses for the year ended January 31, 2007, together with their supporting documents. Below are the details:

SUMMARY OF TAXES AND LICENSES AND MISCELLANEOUS CHARGES				
DATE	**REF. NO.**	**PAYEE**	**PARTICULARS**	**AMOUNT**
16-Feb-06	O.R. No. 0388408	City of Makati	Real Property Tax	₱312,864.33[63]
01-Apr-06	B.S. No. 178195	Pacific Star Bldg., Condo. Corp.	Real Property Tax for 2nd Qtr 2006	108,566.80[64]
Total				₱ 421,431.13
Less: Adjustments				19,314.13
Balance, 31-Jan-07				**₱402,117.00**

Falling within the purview of Sections 34(A)(1) and (C)(1) of the NIRC of 1997, petitioner is correct in claiming the above-listed expenses as deductions. That being said, respondent has no basis for disallowing said expenses.

[61] Exhibit "D".
[62] Exhibit "O-1".
[63] Exhibit "O-4-g", Docket, p. 638.
[64] Exhibit "O-4-h", Docket, p. 639

B. Disallowance of Unsupported Share in Home Office Expenses – ₱1,467,064.00

Respondent disallowed the purported unsupported share in home office expenses in the amount of ₱1,467,064.00 that was claimed by petitioner in its Tentative Income Tax Return.[65]

The Court finds the disallowance without factual basis. Examination of the Final Income Tax Return for the fiscal year ended January 31, 2007 reveals that petitioner did not claim this item as one of the deductions.[66] As such, it is unnecessary for respondent to require petitioner to produce additional supporting documents related to such expense.

C. Non-applicability of the Prior Year's Excess Tax Credits – ₱186,819.00

Respondent disallowed the application of prior year's excess tax credits for the fiscal year ended January 31, 2007 in the amount of ₱186,819.00 against the assessed deficiency income tax, alleging that the same has been carried over to the succeeding year.[67]

Since petitioner had no taxable income for the fiscal year ended January 31, 2007, petitioner has the right to carry over the excess tax credits for the fiscal year ended January 31, 2007 to the subsequent taxable periods.[68]

Moreover, respondent cannot disallow the same on the ground that it was already carried forward to the succeeding

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[65] Par. 63, Petitioner's Memorandum, Docket, p. 951.
[66] Exhibit "E-6", Docket, p. 565.
[67] Par. 66, Petitioner's Memorandum, Docket, p. 951.
[68] Par. 67, Petitioner's Memorandum, Docket, p. 951.

year because any tax benefit derived by petitioner from the carry-over of the said amount redounds to the succeeding fiscal year ending January 31, 2008. Since the tax benefit will be in the succeeding fiscal year, at most, petitioner may only be assessed in the said succeeding year.

II. DEFICIENCY VALUE-ADDED TAX

The deficiency VAT assessment was computed as follows:[69]

Rental Income per FS	₱5,527,704.00
Output Tax	663,324.48
Less: Tax Paid/Input Tax	
VAT Paid per Return	561,274.58
Basic Tax Due	102,049.90
Add: Interest (02.26.07 to 12.10.10)	77,334.25
TOTAL AMOUNT DUE	**₱179,384.15**

Upon verification, petitioner is correct in its allegation that respondent's assessment was erroneous as the deficiency VAT assessment was computed based on the Rental Income appearing in the Tentative Financial Statements.

Likewise, from the reconciliation below, it can be deduced that petitioner has correctly paid its VAT on rentals based on gross receipts as reported in its Annual Income Tax Return[70] and Audited Financial Statements.[71]

MONTH	VAT PAYMENT	EXHIBIT
February 2006	₱ 51,024.96	"F-1"
March	102,049.93	"G-1"
April	-	
May	-	
June	153,074.88	"H-1"
July	-	

[69] Exhibit "V", Docket, p. 727.
[70] Exhibit "E", Line 14c, Docket, p. 549.
[71] Exhibit "O-2-e-4", Docket, p. 608.

August	102,049.92	"K-1"
September	51,024.96	"L-1"
October	-	
November	102,049.93	"M-1"
December	-	
January 2007	-	
Total Amount Paid	**₱ 561,274.59**	
	12%	
Rental Income	**₱4,677,288.25**	"O-2-E-4"

The gross rental income can be computed by dividing the total VAT payments by 12% VAT rate. The resulting gross rental income of ₱4,677,288.25 tallied with that reported in the Audited Financial Statements. Further, it can be inferred that such payment made by petitioner was equivalent to 12% since at the time the VAT due was paid, the 12% rate of VAT has already been implemented, as provided under Section 108(A) of the NIRC of 1997, as amended, and as implemented by Section 9 of Revenue Regulations No. 04-07, which read:

> "SEC. 108. *Value-added Tax on Sale of Services and Use or Lease of Properties.* –
>
> (A) *Rate and Base of Tax.* - There shall be levied, assessed and collected, a value-added tax equivalent to ten percent (10%) of gross receipts, derived from the sale or exchange of services, including the use or lease of properties: *Provided*, That the President, upon the recommendation of the Secretary of Finance, shall, effective January 1, 2006, raise the rate of value-added tax to twelve percent (12%), xxx"
>
> "SECTION 9. *VAT on the Sale of Services and Use or Lease of Properties.* - Sec. 4.108-1 of RR No. 16-2005 is hereby amended to read as follows:

> 'SEC. 4.108-1. *VAT on the Sale of Services and Use or Lease of Properties*. - Sale or exchange of services, as well as the use or lease of properties, as defined in Sec. 108(A) of the Tax Code shall be subject to VAT, equivalent to **twelve percent (12%)** of the gross receipts (excluding VAT) **starting February 1, 2006**.'" *(Emphasis supplied)*

III. INCREMENTS FOR LATE FILING/PAYMENT OF VAT RETURN FOR MARCH 2006

Petitioner claimed that it filed the VAT Return and paid the tax due thereon less than one week after the last day for payment of the VAT Return for March 2006. Due to the late filing/payment of its VAT Return for March 2006, respondent assessed petitioner for 25% surcharge and 20% interest in the amount of ₱25,512.48 and ₱335.51, respectively. According to petitioner, since it voluntarily filed the VAT Return, the imposition of the 25% surcharge is unjust and unduly excessive.[72]

The Court finds petitioner's allegation untenable.

The pertinent provisions of the NIRC of 1997 and Revenue Regulations No. 16-2005 with regard to the filing and payment of VAT are quoted hereunder:

> "SEC. 114. *Return and Payment of Value-added Tax*. –

[72] Pars. 38 to 40, Petition, Docket, p. 11.

(A) *In General.* – Every person liable to pay the value-added tax imposed under this Title shall **file a quarterly return of the amount of his gross sales or receipts within twenty-five (25) days following the close of each taxable quarter** prescribed for each taxpayer: *Provided, however,* That VAT-registered persons shall pay the value-added tax on a monthly basis." *(Emphasis supplied)*

"SECTION 4.114-1. *Filing of Return and Payment of VAT.* -

(A) *Filing of Return.* - Every person liable to pay VAT shall **file a quarterly return of the amount of his quarterly gross sales or receipts within twenty five (25) days following the close of taxable quarter** using the latest version of Quarterly VAT Return. The term 'taxable quarter' shall mean the quarter that is synchronized to the income tax quarter of the taxpayer (*i.e.*, the calendar quarter or fiscal quarter)." *(Emphasis supplied)*

Records prove that petitioner did not file its Monthly VAT Return for the month of March 2006; it instead filed a Quarterly VAT Return for the first quarter of 2006 covering the period January to March 2006. A scrutiny of the records would also show that petitioner filed its Quarterly VAT Returns on a calendar year basis, *viz.*, on the quarter ending March 31,[73] June 30[74] and September 30[75] of 2006. As such, the VAT liability for the first quarter ending March 31, 2006, which can be surmised as the subject of the present assessment, should have been filed and paid on or before April 25, 2006.

However, as can be gleaned from the same records, petitioner filed its Quarterly VAT Return and paid its VAT

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[73] Exhibit "G".
[74] Exhibit "I".
[75] Exhibit "L".

liability for the first quarter ending March 2006 in the amount of ₱102,049.93 only on May 2, 2006. Thus, for being belatedly remitted, the same shall be imputed with interest computed from April 25, 2006 until May 2, 2006, pursuant to Section 249(A) of the NIRC of 1997, which states:

> "SEC. 249. *Interest*. -
>
> (A) *In General*. - There shall be assessed and collected on any unpaid amount of tax, **interest at the rate of twenty percent (20%) per annum**, or such higher rate as may be prescribed by rules and regulations, from the date prescribed for payment until the amount is fully paid." *(Emphasis supplied)*

Similarly, for its failure to file the VAT Return and to pay its VAT liability on the date prescribed, petitioner shall be subjected to 25% surcharge, in addition to the tax required to be paid, in accordance with Section 248(A)(1) of the NIRC of 1997, to wit:

> "SEC. 248. *Civil Penalties*. –
>
> (A) There shall be imposed, in addition to the tax required to be paid, a penalty equivalent to **twenty-five percent (25%) of the amount due**, in the following cases:
>
> (1) **Failure to file any return and pay the tax due thereon** as required under the provisions of this Code or rules and regulations **on the date prescribed**;" *(Emphasis supplied)*

Consequently, petitioner shall be held liable to pay the amounts of ₱25,512.48 and ₱391.42, representing 25% surcharge and 20% interest or in the aggregate amount of ₱25,903.90, as computed below:

Basic Tax Due			₱ 102,049.93
Add:	Surcharge (25%)	₱ 25,512.48	
	Interest (04.25.06 to 5.02.06)	391.42	25,903.90
Total			₱ 127,953.83
Less:	Amount Remitted		102,049.93
Tax Due			**₱25,903.90**

IV. COMPROMISE PENALTY

Respondent imposed compromise penalty against petitioner in the amount of ₱33,400.00, broken down as follows:[76]

VIOLATION	AMOUNT OF SUGGESTED COMPROMISE PENALTY
Non-Filing of Monthly Remittance Return of Creditable Income Taxes Withheld (Expanded)	₱ 2,400.00
Late Filing and Payment of VAT due for the Month of March 2006	16,000.00
Failure to register/keep books of accounts	15,000.00
TOTAL	**₱33,400.00**

Petitioner disagreed with the imposition of the compromise penalty in its protest letters, and requested the reduction or waiver of the same. Since petitioner did not consent to the imposition of compromise penalty against it, petitioner asserted that respondent cannot demand payment of the compromise penalty.

Compromise is a penalty to avoid prosecution for violation of the provisions of the Tax Code.[77] Pursuant to Revenue Memorandum Order (RMO) No. 01-90, as amended by RMO No. 19-07, compromise penalties are amounts suggested in settlement of criminal liability, and may not be imposed or exacted on the taxpayer in the event the

[76] Par. 41, Petition, Docket, p. 11.
[77] *Philippine International Fair, Inc. vs. Collector of Internal Revenue, et. al.,* G.R. No. L-12928 and G.R. No. L-12932, March 31, 1962.

taxpayer refuses to pay the same. Clearly, the compromise penalty implies a mutual agreement between the parties in respect to the thing or subject matter which is so compromised. The imposition of the compromise penalty without the conformity of the taxpayer is illegal and unauthorized.[78] In this case, there is nothing in the records which would show that petitioner consented to the compromise penalties. *Ergo*, the compromise penalties should not be imposed and must be cancelled.

WHEREFORE, premises considered, the instant Petition is hereby **PARTIALLY GRANTED**. The assessments issued by respondent against petitioner covering deficiency income tax, value-added tax and compromise penalty are hereby **CANCELLED** and **SET ASIDE**. On the other hand, the assessment for increments for late filing of the VAT Return for March 2006 is hereby **UPHELD** with modification. Accordingly, petitioner is hereby **ORDERED** to **PAY** the amount of **₱25,903.90** representing increments for late filing of the VAT Return for March 2006. Petitioner is likewise **ORDERED** to **PAY** delinquency interest at the rate of 20% per annum on the amount of ₱25,903.90, computed from December 10, 2010 until full payment thereof pursuant to Section 249(C) of the NIRC of 1997.

SO ORDERED.

Cielito N. Mindaro-Grulla
CIELITO N. MINDARO-GRULLA
Associate Justice

WE CONCUR:

ROMAN G. DEL ROSARIO
Presiding Justice

ERLINDA P. UY
Associate Justice

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[78] *Commissioner of Internal Revenue vs. Lianga Bay Logging Co. Inc., et. al.*, G.R. No. 35266, January 21, 1991.

CERTIFICATION

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

ROMAN G. DEL ROSARIO
Presiding Justice
Chairperson, First Division