REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
Quezon City

Third Division

FRUITS & DAIRY SOMMELIER INC.,
Petitioner,

- versus -

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

CTA CASE NO. 9720

Members:

UY, *Chairperson*
RINGPIS-LIBAN, *and*
MODESTO-SAN PEDRO, *JJ.*

Promulgated:
MAY 28 2021
3:24 p.m.

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DECISION

RINGPIS-LIBAN, J.:

The Case

This case involves a *Petition for Review* filed by Petitioner Fruits & Dairy Sommelier, Inc. ("FDSI") against Respondent Commissioner of Internal Revenue on November 21, 2017, praying for the cancellation of the *Final Assessment Notice* ("FAN") dated January 13, 2017 issued against the Petitioner for alleged deficiency income tax, value-added tax ("VAT"), expanded withholding tax ("EWT"), documentary stamp tax ("DST"), improperly accumulated earnings tax ("IAET"), and compromise penalty, for taxable year 2013, in the aggregate amount of Php5,759,540.75.[1]

The Facts

Petitioner FDSI is a corporation duly organized and existing under and by virtue of the laws of the Republic of the Philippines, with office address

[1] Docket, Pre-Trial Order dated August 15, 2018, Statement of the Case, p. 169.

Bicutan, Taguig City.[2] It is a registered with the Bureau of Internal Revenue ("BIR") with Taxpayer Identification Number ("TIN") 007-214-571-00000.[3]

Respondent is the duly-appointed Commissioner of Internal Revenue, 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, grant tax refunds and issue tax credit certificates, pursuant to the provisions of the National Internal Revenue Code ("NIRC") of 1997, as amended, and other tax laws, rules and regulations.[4]

On December 11, 2015, Petitioner received the BIR's *Letter of Authority* ("LOA") No. eLA 201200036513 dated December 04, 2015,[5] authorizing Revenue Officer ("RO") Mary Ann Zamuco and Group Supervisor ("GS") Frederico Pilarca of Revenue District Office ("RDO") No. 44 – Taguig-Pateros, to examine Petitioner's books of accounts and other accounting records for all internal revenue taxes, covering the period from January 01, 2013 to December 31, 2013.

Thereafter, Respondent issued the *Preliminary Assessment Notice* ("PAN") dated December 28, 2016,[6] informing Petitioner that after investigation, there has been found from the latter income tax, VAT, EWT, DST, IAET, and compromise penalty, in the aggregate amount of Php5,692,146.97.

On January 13, 2017, Respondent issued the assailed FAN, with *Details of Discrepancies* and *Assessment Notices*,[7] assessing Petitioner for deficiency income tax, VAT, EWT, DST, IAET, and compromise penalty, in the aggregate amount of Php5,759,540.75.

Petitioner filed its letter dated February 23, 2017 on February 24, 2017,[8] protesting against the subject tax assessments. Subsequently, Petitioner transmitted the supporting documents to its protest on April 25, 2017 *via* the letter dated April 24, 2017.[9]

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[2] *Id.,* Joint Stipulation of Facts and Issues (JSFI), Facts Admitted, Par. 1, p. 151; Exhibit "P-2", pp. 196 to 206.

[3] *Id.,* Exhibit "P-1", p. 195.

[4] *Id.,* JSFI, Facts Admitted, Par. 2, p. 151.

[5] BIR Records, Exhibit "R-1", p. 45.

[6] *Id.,* Exhibit "R-7", pp. 414 to 418.

[7] Docket, Exhibits "P-20" to "P-26-A", pp. 387 to 399; BIR Records, Exhibit "R-9", pp. 443 to 454.

[8] Docket, Exhibit "P-27", pp. 400 to 407.

[9] *Id.,* Exhibit "P-28", Docket, pp. 408 to 410.

On November 21, 2017, the instant *Petition for Review* was filed.[10] The case was originally raffled to this Court's First Division.

Respondent posted his *Answer* on January 26, 2018,[11] interposing the following special and affirmative defenses, to wit:

> "**3.** He reiterates and repleads the preceding paragraphs of this answer as part of his Special and Affirmative Defenses;
>
> **4.** Petitioner was assessed for deficiency income tax, value-added tax, expanded withholding tax, documentary stamp tax, improperly accumulated earnings tax and compromise penalty for taxable year 2013 for the reason that during the administrative investigation of its tax case by the Bureau of Internal Revenue (BIR), Petitioner failed to substantiate or submit supporting evidence against the BIR findings, more specifically shown under the Details of Discrepancies attached to the Preliminary Assessment Notice (PAN) dated December 28, 2016 and Formal Assessment Notice (FAN) dated January 13, 2017 which are briefly discussed hereunder, viz:
>
> **INCOME TAX;**
>
> **A.) Disallowed Expenses due to non-withholding amounting to P1,066,441.89:**
>
> - Verification disclosed that Petitioner did not withhold the appropriate withholding tax due on various local payments. Section 34 (K) of the NIRC, as amended, expressly provides that '. . . any amount paid or payable which is otherwise deductible from, or taken into account in computing the gross income or for which depreciation or amortization maybe allowed under this Section, shall be allowed as a deduction only *if it is shown that the tax required to be deducted and withheld therefrom has been paid to the Bureau of Internal Revenue* in accordance this Section of this Code . . .' Hence, the aforementioned expenses have been disallowed pursuant to the above provision of the law.
>
> **VALUE ADDED TAX (VAT);**

[10] *Id.,* pp. 10 to 23.
[11] *Id.,* pp. 58 to 64.

B.) Input Tax on Capital Goods Deferred to Succeeding Period amounting to P240,142.85:

- The input tax on Capital Goods deferred to succeeding period amounting to P240,142.85 was not applied against the allowable input tax in computing deficiency value added tax since this shall spread evenly over the month of acquisition and the fifty-nine (59) succeeding months pursuant to Section 110 (A) of the Tax Code.

C.) Disallowed Input Tax Allocated to Exempt Sales amounting to P1,991,772.99:

- Verification disclosed that Petitioner failed to allocate input tax on the exempt sales of P53,617,547.84 hence input tax in the amount of P1,991,772.99 allocated to exempt sales has been disallowed pursuant to Section 4.110-4(2). 'If any input tax cannot be directly attributed to either a VAT taxable or VAT-exempt transaction, the input tax shall be pro-rated to the VAT taxable and VAT-exempt transactions and only the vatable portion pertaining the transaction subject to VAT may be recognized for the input tax credit.'

D.) Input Tax Carried Forward to Succeeding Period/Quarter amounting to P184,229.82:

- The excess input tax amounting to P184,229.82 was not applied against the output tax in computing deficiency value added tax since this shall be carried over to the next succeeding period/quarter(s) as provided under Section 110(B) of the Tax Code, as amended.

EXPANDED WITHHOLDING TAX

E.) Basic Tax Due amounting to P190,547.77: - Since Petitioner failed to withhold/remit the correct withholding tax due on several income payments previously disallowed as deductions from gross income, Petitioner is still liable to pay the deficiency withholding tax thereon pursuant to Section 2.57.2 of Revenue Regulations No. 2-98, as amended.

DOCUMENTARY STAMP TAX

F.) Basic Documentary Stamp Tax Due amounting to P37,000.00:

- Verification disclosed that Petitioner failed to file and pay the documentary stamp tax due on their related parties hence assessed pursuant to Section 179 of the NIRC as amended.

IMPROPERLY ACCUMULATED EARNINGS TAX

G.) Basic Tax Due amounting to P974,860.90

- Verification disclosed that an improperly accumulation of earnings is present in the records of the company, hence subject to IAET pursuant to Sec. 29 of the NIRC, as amended.

Likewise, it was disclosed that Petitioner failed to comply on time, as required by existing revenue laws rules and regulations, in relation to Section 255 of the National Internal Revenue Code as amended by R.A. 8424 which states;

> 'Sec. 255 – Failure to File Return, Supply Correct and Accurate Information, Pay Tax, Withhold and Remit Tax and Refund Excess Taxes Withheld Taxes Withheld on Compensation – Any person required under this Code or by rules and regulations promulgated thereunder to pay any tax, make a return, keep any record, or supply correct and accurate information, who willfully fails to pay such tax, make such returns keep such record, or supply such correct and accurate information, or withhold or remit taxes withheld, or refund excess taxes withheld on compensation, at the time or times required by law or rules and regulations shall, in addition to other penalties provided by law, upon conviction thereof, be punished by a fine of not less than Ten thousand pesos (P10,000.00) and suffer imprisonment of not less than one (1) year but not more than ten (10) years.'

5. In the landmark case of **Aznar vs. Court of Tax Appeals and Collector of Internal Revenue (G.R. No. L-**

20569, August 23, 1974) the Supreme Court stated that a false return is one which contains wrong information due to mistake, carelessness or ignorance. The word 'false' is defined as an adjective which means not true or not correct. Intent to evade is immaterial in case of filing false returns. As long as there is some deviation from the truth, whether it is due to mistake, ignorance or carelessness, falsity arises.

6. Petitioner interposes prescription so as to exculpate it from its tax liabilities. To that, suffice it to state that allegations of prescription must be clearly shown. Since prescription is one of the affirmative defenses of the taxpayer, 'it is incumbent upon [it] to positively establish when the prescriptive period started to run and where the same ended.' **(Taligaman Lumber Co. v. Collector, G.R. No. L-15716, March 31, 1962)**

In relation thereto, this Court sitting En Banc in the case of **CDL Hotels (Phils.) Corporation vs. CIR, CTA EB Case No. 339, August 10, 2009**, held that:

> 'While the prescriptive period for assessment is three years as prescribed under section 203 of the 1997 NIRC, as amended; however, Section 222 of the 1997 NIRC provided for exceptions to the period of limitation of assessment and collection of taxes. We quote:
>
>> 'SEC. 222. Exceptions as to Period of Limitation of Assessment and Collection of Taxes. –
>>
>> (a) In case of a false or fraudulent return with intent to evade tax or of failure to file a return, the tax may be assessed, or a proceeding in court for the collection of such tax may be filed without assessment, at any time within (10) years after the discovery of the falsity, fraud or omission: ...;
>>
>> (b) If before the expiration of the time prescribed in Section 203 for the assessment of the tax, both the Commissioner and the taxpayer have agreed in writing to its assessment after

> such time, the tax may be assessed within the period agreed upon. The period so agreed upon may be extended by a subsequent written agreement made before the expiration of the period previously agreed upon.
>
> xxx xxx xxx'

A reasonable understanding of the foregoing law is that false return is different from fraudulent return with intent to evade tax or from failure to file a return. The above provision should be interpreted to mean a separation of the three different situations of false return, fraudulent return with intent to evade tax, and failure to file a return. The difference between 'false return' and 'fraudulent return' cannot be denied. While the first merely implies deviation from the truth, whether intentional or not, the second implies intentional or deceitful entry with intent to evade the taxes due. The ordinary period of prescription of 3 years within which to assess tax liabilities under Sec. 203 of the 1997 NIRC, as amended, should be applicable to normal circumstances; but whenever the government is placed at a disadvantage so as to prevent its lawful agents from proper assessment of tax liabilities due to false returns, fraudulent returns intended to evade payment of tax or failure to file returns, the period of ten years as provided for in Section 222 of the 1997 NIRC, as amended, from the time of the discovery of the falsity, fraud or omission even seems to be inadequate and should be the one enforced.

In the case at bar, although Petitioner filed its monthly return as mandated by law, it failed to declare thereto the income subject to the tax under the belief that the income supposedly subject to the withholding tax is not an income but a deductible expense. The returns filed by Petitioner can be considered as false return because it deviated from the truth when no income was declared, when in truth there was an income subject tot tax. Being considered as false return, it is immaterial if

> Petitioner intentionally omitted to declare its income subject to final withholding tax or not.
>
> **Considering that Petitioner's return is false, the applicable prescriptive period would be ten years from the discovery of falsity.** In the case at bar, the latest return filed was on January 11, 1999, while the FAN was issued on January 29, 2002, such period being within the ten-year period it follows that the assessment had not yet prescribed.
>
> Moreover, the Supreme Court had ruled that **the filing of deficient returns which prevent the Commissioner of Internal Revenue from computing the proper taxes is tantamount to non-filing. The Commissioner had to determine and assess the taxes on data obtained, not from the return, but from other sources. Hence, the assessment for deficiency final withholding tax, therefore, has not prescribed**.' (Emphasis supplied)

Applying the foregoing rule and jurisprudence in the case at bar, a close scrutiny of the returns filed by Petitioner clearly revealed that declaration made therein were substantially deficient in amount and did not disclose the truth regarding the correct amount of income subject to tax compared to the amount remitted to the BIR. These falsities arising in Petitioner's returns provide ample basis for the application of the 10-year prescriptive period.

7. The Preliminary Assessment Notice and Formal Assessment Notice were served to the Petitioner through registered mail

8. The assessment issued against Petitioner for deficiency income tax, value-added tax, expanded withholding tax, documentary stamp tax, improperly accumulated earnings tax and compromise penalty for taxable year 2013 were made in accordance with law and regulations;

9. Assessment are *prima facie* presumed correct and made in good faith. The taxpayer has the duty of proving otherwise. In the absence of proof of any irregularities in the performance of official duties, an assessment will not be disturbed

***(Aban, Law of Baisc Taxation in the Philippines, 1st Edition, p. 109)*".**

The Pre-Trial Conference was initially set on April 05, 2018.[12] Upon separate motions of the parties,[13] the Pre-Trial Conference was eventually reset to, and held on, July 5, 2018.[14] Prior thereto, *Petitioner's Pre-Trial Brief* was filed on March 28, 2018;[15] while *Respondent's Pre-Trial Brief* was submitted on June 28, 2018.[16]

Respondent forwarded the *BIR Records* on July 2, 2018.[17]

The parties submitted their *Joint Stipulation of Facts and Issues* on July 16, 2018.[18] The Court approved the said JSFI and deemed the termination of the Pre-Trial in its Resolution dated July 27, 2018.[19] Thereafter, the Pre-Trial Order dated August 15, 2018 was issued by the Court.[20]

Trial then ensued.

During trial, Petitioner presented its documentary and testimonial evidence. Petitioner offered the sole testimony of Ms. Rosalie Tanguanco,[21] Petitioner's authorized representative for tax and financial matters. Considering that Respondent did not file a manifestation on whether he will conduct a cross-examination on Petitioner's witness,[22] his right to cross-examine the latter was deemed waived.[23]

Pursuant to the Order dated September 26, 2018,[24] the instant case was transferred to this Court's Third Division.

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12 *Id.,* Notice of Pre-Trial Conference dated February 09, 2018, pp. 66 to 67.

13 *Id.,* Respondent's Urgent Motion to Reset, pp. 68 to 69; Petitioner's Motion to Reset Pre-Trial Conference, pp. 89 to 91.

14 *Id.,* Order dated April 2, 2018, p. 87; Order dated April 13, 2018, p. 94; Order dated July 5, 2018, pp. 140 to 142.

15 *Id.,* pp. 72 to 77.

16 *Id.,* pp. 96 to 98.

17 *Id.,* Compliance dated June 27, 2018, p. 138.

18 *Id.,* pp. 151 to 156.

19 *Id.,* p. 163.

20 *Id.,* pp. 169 to 177.

21 *Id.,* Exhibit "P-29", pp. 80 to 86, and 412 to 418; Minutes of the hearing held on, and Order dated, August 30, 2018, pp. 178 to 181.

22 *Id.,* Records Verification Report dated November 23, 2018 issued by the Judicial Record Division of this Court, p. 184.

23 *Id.,* Resolution dated December 04, 2018, p. 186.

24 *Id.,* p. 182.

On December 14, 2018, Petitioner filed its *Formal Offer of Evidence.*[25] Respondent posted his *Comment to Petitioner's Formal Offer of Evidence* on December 17, 2018.[26] In the Resolution dated February 26, 2019,[27] the Court admitted Petitioner's Exhibits.

For his part, Respondent presented his documentary and testimonial evidence. He proffered the testimony of Ms. Jocelyn C. Quevedo,[28] Respondent's Revenue Officer II.

Respondent submitted his *Formal Offer of Evidence* on November 07, 2019.[29] Petitioner filed its *Comment (to Respondent's Formal Offer of Evidence)* on November 12, 2019.[30] In the Resolution dated February 04, 2020,[31] the Court admitted Respondent's Exhibits.

The *Memorandum (for Petitioner)* was filed on March 04, 2020.[32] Respondent, however, failed to file his memorandum.[33]

The instant case was deemed submitted for decision on September 23, 2020.[34]

The Issues

The following are the issues stipulated by the parties for the Court's determination, *viz*:

> "1. Whether Petitioner is liable to pay the aggregate amount of **P5,719,540.75**[]representing alleged income tax (IT) – IT-ELA36513-13-17-181; value added tax (VAT) – VT-ELA36513-13-17-181; expanded withholding tax (EWT) - WE-ELA36513-13-17-181; documentary stamp tax (DST) – DS-ELA36513-13-17-181; Improperly Accumulated Earnings Tax

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25 *Id.,* pp. 187 to 194.
26 *Id.,* pp. 419 to 420.
27 *Id.,* 425 to 426.
28 *Id.,* Exhibit "R-11", pp. 100 to 107; Minutes of the hearing held on, and Order dated, October 24, 2019, pp. 429 to 431.
29 *Id.,* pp. 432 to 436.
30 *Id.,* pp. 440 to 442.
31 *Id.,* pp. 446 to 447.
32 *Id.,* pp. 448 to 480.
33 *Id.,* Records Verification Report dated September 10, 2020 issued by the Judicial Records Division of this Court, p. 482.
34 *Id.,* Resolution dated September 23, 2020, p. 484.

(IAET) - IE- ELA36513-13-17-181; and Compromise Penalty – MC- ELA36513-13-17-181, for taxable year 2013.

2. Whether the FAN dated January 13, 2017 issued against Petitioner representing alleged tax deficiencies for taxable year 2013 and the right of the Government through the Bureau of Internal Revenue to collect such alleged deficiency taxes had prescribed pursuant to Section 203 and 222 of the 1997 Tax Code, as amended."[35]

Petitioner's Arguments

Petitioner argues that the absence of a validly issued LOA to conduct the audit rendered the assessment void; that this Court has the power to resolve the issue on the validity of the authority of revenue examiners to conduct the audit leading to the present assessment; that Respondent's failure to issue a PAN, as prescribed under Section 228 of the 1997 NIRC, as amended, and Revenue Regulations ("RR") No. 12-99, is a denial of due process; that the present assessment is barred by prescription; and that the FAN dated January 13, 2017 did not set and fix the tax liability, which is still subject to modification or adjustment.

Respondent's Counter-arguments

In the *Answer*, Respondent avers that Petitioner filed a false return, thus, the ten-year prescriptive period to assess the latter for deficiency taxes shall be applied; and that the PAN and FAN were served to Petitioner through registered mail.

Discussion/Ruling

The instant *Petition for Review* has merit.

The Court may rule on the validity or scope of the authority of the revenue examiners to conduct the audit leading to the subject tax assessments.

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[35] *Id.*, JSFI, Issues, p. 152.

Section 1, Rule 14 of the 2005 Revised Rules of the Court of Tax Appeals ("RRCTA") reads as follows:

"RULE 14
JUDGMENT, ITS ENTRY AND EXECUTION

SECTION 1. – *Rendition of judgment* – xxx

In deciding a case, the Court may not limit itself to the issues stipulated by the parties but may also rule upon related issues necessary to achieve an orderly disposition of the case."[36]

Such power of this Court is confirmed and recognized by the Supreme Court in the case of *Commissioner of Internal Revenue v. Lancaster Philippines, Inc.,*[37] *viz:*

"**On whether the CTA can resolve an issue which was not raised by the parties, <u>we rule in the affirmative</u>.**

Under Section 1, Rule 14 of A.M. No. 05-11-07-CTA, or the Revised Rules of the Court of Tax Appeals, the CTA is not bound by the issues specifically raised by the parties but may also rule upon related issues necessary to achieve an orderly disposition of the case. The text of the provision reads:

SECTION 1. *Rendition of judgment.* – xxx

In deciding the case, the Court may not limit itself to the issues stipulated by the parties but may also rule upon related issues necessary to achieve an orderly disposition of the case.

The above section is clearly worded. On the basis thereof, the CTA Division was, therefore, well within its authority to consider in its decision the question on the scope of authority of the revenue officers who were named in the LOA <u>even though the parties had not raised the same in their pleadings or memoranda</u>. The CTA En Banc was

[36] *Emphasis supplied.*
[37] G.R. No. 183408, July 12, 2017.

> likewise correct in sustaining the CTA Division's view concerning such matter."[38]

Thus, the issue of whether the ROs who examined or audited Petitioner has valid authority to do so, and such other issues necessary to achieve an orderly disposition of the case, may be resolved by the Court, even when not specifically raised by the parties.

The revenue officers, who conducted the tax investigation or audit of Petitioner, had no valid authority to conduct the said investigation/audit. Thus, the subject tax assessments are void.

The audit process in the BIR normally commences with the issuance by Respondent or his duly authorized representative of an LOA. The LOA gives notice to the taxpayer that it is under investigation for possible deficiency tax assessment; at the same time, it authorizes or empowers a designated RO to examine, verify, and scrutinize a taxpayer's books and records, in relation to internal revenue tax liabilities for a particular period.[39]

The power to issue an LOA by Respondent or his duly authorized representative is derived from Section 6(A) of the NIRC of 1997, as amended, which provides as follows:

> "SEC. 6. *Power of the Commissioner to Make Assessments and Prescribe Additional Requirements for Tax Administration and Enforcement.* –
>
> (A) *Examination of Returns and Determination of Tax Due.* - After a return has been filed as required under the provisions of this Code, **the Commissioner or his duly authorized representative may authorize the examination of any taxpayer and the assessment of the correct amount of tax**: *Provided, however*, That failure to file a return shall not prevent the Commissioner from authorizing the examination of any taxpayer." [40]

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[38] *Emphasis and underscoring supplied.*

[39] Commissioner of Internal Revenue v. Lancaster Philippines, Inc., G.R. No. 183408, July 12, 2017.

[40] *Emphasis and underscoring supplied.*

Based on the foregoing provision, an authority emanating from Respondent or his duly authorized representative is required **before an examination and an assessment may be made against a taxpayer.**

Relative thereto, Section 13 of the NIRC of 1997 provides that the authority of an RO to examine or to recommend the assessment of any deficiency tax due must be exercised pursuant to an LOA, to wit:

> "SEC. 13. *Authority of a Revenue Officer.* – Subject to the rules and regulations to be prescribed by the Secretary of Finance, upon recommendation of the Commissioner, **a Revenue Officer assigned to perform assessment functions in any district may, pursuant to a Letter of Authority issued by the Revenue Regional Director, examine taxpayers within the jurisdiction of the district in order to collect the correct amount of tax, or to recommend the assessment of any deficiency tax due** in the same manner that the said acts could have been performed by the Revenue Regional Director himself.[41]

Thus, a grant of authority, through an LOA, must be made assigning an RO, to perform tax assessment functions, in order that such officer may examine taxpayers and collect the correct amount of tax, or to recommend the assessment of any deficiency tax due.

A reading of Section 7 of the NIRC of 1997, as amended, shows that the issuance of an LOA is not one of the non-delegable powers of the Comissioner of Internal Revenue, *viz:*

> "SEC. 7. **Authority of the Commissioner to Delegate Power.** – The Commissioner may delegate the powers vested in him under the pertinent provisions of this Code to any or such subordinate officials with the rank equivalent to a division chief or higher, subject to such limitations and restrictions as may be imposed under rules and regulations to be promulgated by the Secretary of Finance, upon recommendation of the Commissioner: Provided, however, That the following powers of the Commissioner shall not be delegated:
>
> (a) The power to recommend the promulgation of rules and regulations by the Secretary of Finance;

[41] *Emphasis and underscoring supplied.*

(b) The power to issue rulings of first impression or to reverse, revoke or modify any existing ruling of the Bureau;

(c) The power to compromise or abate, under Sec. 204 (A) and (B) of this Code, any tax liability: Provided, however, That assessments issued by the regional offices involving basic deficiency taxes of Five hundred thousand pesos (P500,000) or less, and minor criminal violations, as may be determined by rules and regulations to be promulgated by the Secretary of finance, upon recommendation of the Commissioner, discovered by regional and district officials, may be compromised by a regional evaluation board which shall be composed of the Regional Director as Chairman, the Assistant Regional Director, the heads of the Legal, Assessment and Collection Divisions and the Revenue District Officer having jurisdiction over the taxpayer, as members; and

(d) The power to assign or reassign internal revenue officers to establishments where articles subject to excise tax are produced or kept."

On the contrary, issuing LOAs is a delegable power which the Commissioner of Internal Revenue may devolve to Revenue Regional Directors, as expounded on in Section 10 of the NIRC of 1997, as amended:

"SEC. 10. **Revenue Regional Director.** – Under rules and regulations, policies and standards formulated by the Commissioner, with the approval of the Secretary of Finance, the Revenue Regional director shall, within the region and district offices under his jurisdiction, among others:

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(c) **<u>Issue</u> <u>Letters</u> <u>of</u> <u>authority</u> <u>for</u> <u>the</u> <u>examination</u> <u>of</u> <u>taxpayers</u> within the region**;

xxx

(h) **Perform such other functions as may be provided by law and as may be delegated by the Commissioner**."[42]

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[42] *Emphasis and underscoring supplied.*

To implement said provision, Revenue Memorandum Order ("RMO") No. 36-99[43] was issued, entitled as "Guidelines and Procedures in the Issuance of Letters of Authority, Approval of Audit Reports and Issuance of Assessment Notices and Amending Certain Provisions of Revenue Memorandum Order (RMO) Nos. 26-94, 37-94 and 23-97". The RMO clearly emphasized that it is the Revenue Regional Directors who have the authority to issue LOAs for all audit cases within their regional jurisdiction, *viz*:

"I. OBJECTIVES

1. **To delineate the power to issue Letters of Authority (LAs) to the Revenue Regional Directors pursuant to Sec. 10 (c) of the Tax Code.**

2. To prescribe the revised guidelines and procedures in the issuance of LAs, approval of audit reports and issuance of assessment notices.

II. GUIDELINES AND PROCEDURES

1. Section E of RMO No. 26-94 is hereby amended to read as follows:

The <u>Revenue</u> <u>Regional</u> <u>Director</u> shall approve and sign LAs for all audit cases within his regional jurisdiction...

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2. Section C.2.2.1 of RMO No. 23-97 is hereby amended to read as follows:

The Regional Director shall issue the corresponding Letter of Authority if indications of fraud have been established, and the same has been confirmed by the Regional Tax Fraud Committee (RTFC), composed of the following:

a. Regional Director — Chairman
b. Assistant Regional Director — Vice-Chairman
c. Chief, SID — Member
d. Chief, Assessment Division — Member
e. Chief, Legal Division — Member

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[43] February 09, 1999.

6. The following additional guidelines on the issuance of LAs shall be observed:

6.1 **All LA forms for use by the Revenue District Offices** and Special Investigation Divisions **shall be requisitioned by the Regional Director** from the Accountable Forms Divisions in the National Office.

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6.6 **The Regional Director shall maintain an LA Register for all LAs issued by him.** All issuances, revalidations, cancellations, case closures, assessments and other matters in relation to LAs should be entered in the LA Register. Entries in the LA Register must be complete and updated."[44]

An LOA is, in essence, a contract of agency. Article 1868 of the Civil Code defines agency as a contract where "a person binds himself to render some service or to do something in representation or on behalf of another, with the consent or authority of the latter."

In the case of *Spouses Fernando and Lourdes Viloria v. Continental Airlines, Inc.*[45], the Supreme Court had the occasion to expound on the elements of agency, to wit:

"The elements of agency are: (1) consent, express or implied, of the parties to establish the relationship; (2) the object is the execution of a juridical act in relation to a third person; (3) the agent acts as a representative and not for him/herself; and (4) the agent acts within the scope of his/her authority. **As the basis of agency is representation, there must be, on the part of the principal, an actual intention to appoint, an intention naturally inferable from the principal's words or actions. In the same manner, there must be an intention on the part of the agent to accept the appointment and act upon it.** Absent such mutual intent, there is generally no agency. It is likewise a settled rule that persons dealing with an assumed agent are bound at their peril, if they would hold the principal liable, to ascertain not only the fact of agency but also the nature and extent of authority, and in case either is controverted, the burden of proof is upon them to establish it."[46]

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[44] *Emphasis and underscoring supplied.*
[45] G.R. No. 188288, January 16, 2012.
[46] *Emphasis supplied.*

In an LOA, the Commissioner of Internal Revenue is the principal - as he is the one mandated by the law to make assessments - and the Regional Director, his agent.

Now, may the Regional Director, the Commissioner of Internal Revenue's agent, appoint a sub-agent, in this case, the RO named in the LOA? Article 1892 of the Civil Code says that he can. The said provision states:

> "Art. 1892. **The agent may appoint a substitute if the principal has not prohibited him from doing so**; but he shall be responsible for the acts of the substitute:
>
> (1) When he was not given the power to appoint one;
> (2) When he was given such power, but without designating the person, and the person appointed was notoriously incompetent or insolvent.
>
> All acts of the substitute appointed against the prohibition of the principal shall be void. (1721)"[47]

This power to appoint a sub-agent necessarily includes the power to revoke the same.

Said document where such authority is transferred may be equivalent to an LOA. Several reasons support this. *First*, the only directive under Section 13 of the NIRC of 1997, as amended,[48] which requires that assessment be done by ROs pursuant to an LOA, is that the grant of authority be done ***in writing***. In fact, an "[a]gency may be oral, unless the law requires a specific form."[49]

Second, although the document may not be entitled "Letter of Authority" but otherwise, it can contain all the elements necessary to establish a contract of agency between the Commissioner of Internal Revenue and the new RO. The primary consideration in determining the true nature of a contract is the

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[47] *Emphasis supplied.*

[48] SEC. 13. Authority of a Revenue Officer. - subject to the rules and regulations to be prescribed by the Secretary of Finance, upon recommendation of the Commissioner, a Revenue Officer assigned to perform assessment functions in any district may, **pursuant to a Letter of Authority issued by the Revenue Regional Director**, examine taxpayers within the jurisdiction of the district in order to collect the correct amount of tax, or to recommend the assessment of any deficiency tax due in the same manner that the said acts could have been performed by the Revenue Regional Director himself." (*Emphasis supplied).*

[49] Civil Code of the Philippines, Article 1869.

intention of the parties. If the words of a contract appear to contravene the evident intention of the parties, the latter shall prevail. Such intention is determined not only from the express terms of their agreement, but also from the contemporaneous and subsequent acts of the parties.[50] The title of the contract does not necessarily determine its true nature.[51] In fact, this Court has, time and again, declared certain documents emanating from the Commissioner of Internal Revenue as his "Final Decision" on a Disputed Assessment based on the tenor of the words therein despite the absence of the words "Final Decision" in the title of the document.

In interpreting what a "Letter of Authority" is, as mentioned in Section 13 of the NIRC of 1997, as amended, the laws on contracts and agency embodied in the Civil Code simply cannot be ignored. Every effort must be exerted to avoid a conflict between statutes; so that if reasonable construction is possible, the laws must be reconciled in that manner.[52] Similarly, every new statute should be construed in connection with those already existing and all should be made to harmonize and stand together, if they can be done by any fair and reasonable interpretation. *Interpretare et concordare leges legibus, est optimus interpretandi modus*, which means that the best method of interpretation is that which makes laws consistent with other laws. Tax laws do not exist in a vacuum, and must be appreciated and applied with other laws such as the Civil Code.[53]

The records of this case reveal that after LOA No. eLA 201200036513 dated December , 2015 was issued, authorizing RO Mary Ann Zamuco and GS Frederico Pilarca of RDO No. 44 – Taguig-Pateros, to examine Petitioner's books of accounts and other accounting records for all internal revenue taxes, covering the period from January 1, 2013 to December 31, 2013,[54] Revenue District Officer Florante R. Aninag issued the *Memorandum of Agreement* ("MOA") No. MOA0442015LOA-00005 dated April 04, 2016, referring Petitioner's case/docket to RO Jocelyn C. Quevedo and GS Eulogina E.

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[50] Heirs of Dr. Mario S. Intac and Angelina Mendoza Intac v. Court of Appeals and Spouses Marcelo Roy, Jr. and Josefina Mendoza-Roy and Spouses Dominador Lozada and Martina Mendoza-Lozada, G.R. No. 173211, October 11, 2012 *citing* Spouses Villaceran v. De Guzman, G.R. No. 169055, February 22, 2012; Ramos v. Heirs of Honorio Ramos, Sr., G.R. No. 140848, April 25, 2002, 381 SCRA 594, 601; Heirs of Policronio M. Ureta, Sr. vs. Heris of Liberato M. Ureta, G.R. Nos. 165748 & 165930, September 14, 2011 *citing* Lopez v. Lopez, G.R. No. 161925, November 25, 2009, 605 SCRA 358, 36.

[51] Adelfa Properties, Inc. v. Court of Appeals, G.R. No. 111238, January 25, 1995.

[52] Philippine Amusement and Gaming Corporation (PAGCOR) v. The Bureau of Internal Revenue, represented by Jose Mario Bunag, in his capacity as Commissioner of the Bureau of Internal Revenue, and John Doe and Jane Doe, who are persons acting for, in behalf or under the authority of Respondent, G.R. No. 215427, December 10, 2014, *citing* Lopez v. The Civil Service Commission, 273 Phil. 147, 152 (1991).

[53] Philippine International Trading Corporation v. Commission on Audit, G.R. No. 183517, June 22, 2010.

[54] BIR Records, Exhibit "R-1", p. 45.

Lacson, for the "[c]*ontinuation of the audit/investigation to replace the previously assigned Revenue Officer(s) who...transferred to another district office.*"[55] Petitioner was later informed of the said MOA via the letter dated April 07, 2016 signed by Revenue District Officer Aninag.[56]

Evidence further reveal that upon the recommendation of RO Quevedo and GS Lacson,[57] the BIR issued the PAN dated December 28, 2016 against Petitioner.[58]

Clearly, RO Quevedo and GS Lacson who conducted the examination of Petitioner's records may be deemed authorized to do so without need for a new LOA, only if said letter or notice or memorandum was signed by the Regional Director. In the instant case however, the MOA was only signed by Revenue District Officer Florante R. Aninag. Therefore, RO Quevedo and GS Lacson had no valid authority to conduct tax audit/investigation against Petitioner. Not having the authority to examine Petitioner in the first place, the subject tax assessments are therefore void.

In any event, even granting that there was an LOA issued in favor of RO Quevedo and GS Lacson to conduct the audit of Petitioner, the subject tax assessments are still void, since Petitioner's right to due process was violated by Respondent.

Respondent failed to prove the service of the subject PAN before the issuance of the subject FAN.

In the instant *Petition for Review*, Petitioner denies having received any PAN relative to the present assessment, in violation of its right to due process.

For his part, Respondent points out that the PAN was sent to Petitioner thru registered mail.

However, Respondent's evidence fails to convince this Court that the said PAN was sent or served to Petitioner thru registered mail.

To prove that the service of the subject PAN, Respondent presented the *Transmittal Letter dated December 28, 2018 issued by Philpost.*[59] However, the said

[55] *Id.,* Exhibit "R-2", p. 48.
[56] *Id.,* Exhibit "R-3", p. 50.
[57] *Id.,* Exhibit "R-6", pp. 401 to 403.
[58] *Id.,* Exhibit "R-7", pp. 414 to 418.

document is insufficient so as to show that the same PAN was in fact received by Petitioner.

In *Commissioner of Internal Revenue v. GJM Philippines Manufacturing, Inc.* ("*GJM* case"),[60] the Supreme Court ruled as follows:

> "If the taxpayer denies having received an assessment from the BIR, it then becomes incumbent upon the latter to prove by competent evidence that such notice was indeed received by the addressee. Here, the *onus probandi* has shifted to the BIR to show by contrary evidence that GJM indeed received the assessment in the due course of mail. **It has been settled that while a mailed letter is deemed received by the addressee in the course of mail, this is merely a disputable presumption subject to controversion, the direct denial of which shifts the burden to the sender to prove that the mailed letter was, <u>in fact</u>, received by the addressee.**
>
> **To prove the fact of mailing, it is essential to present the registry receipt issued by the Bureau of Posts or the Registry return card <u>which would have been signed by the taxpayer or its authorized representative</u>.** And if said documents could not be located, the CIR should have, at the very least, submitted to the Court a certification issued by the Bureau of Posts and any other pertinent document executed with its intervention. The Court does not put much credence to the self-serving documentations made by the BIR personnel, especially if they are unsupported by substantial evidence establishing the fact of mailing. **While it is true that an assessment is made when the notice is sent within the prescribed period, <u>the release, mailing, or sending of the same must still be clearly and satisfactorily proved</u>.** Mere notations made without the taxpayer's intervention, notice of control, and without adequate supporting evidence cannot suffice. Otherwise, the defenseless taxpayer would be unreasonably placed at the mercy of the revenue offices."[61]

It is clear that while a mailed letter is deemed received by the addressee in the course of the mail, this is merely a disputable presumption subject to rebuttal. Consequently, the direct denial thereof shifts the burden to the sender

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59 *Id.,* Exhibit "R-8", p. 419.
60 G.R. No. 202695, February 29, 2016.
61 *Emphasis and underscoring supplied.*

to prove that the said letter was *actually* received by the addressee. Furthermore, to prove the fact of mailing, Respondent must present the Registry Receipt issued by the Bureau of Posts or the Registry Return card which would have been signed by the taxpayer or its authorized representative. In the absence of the said documents, a Certification issued by the said Bureau of Posts, *and* any other pertinent document executed with its intervention, must be presented to establish the fact of mailing.

In this case, Petitioner directly denies having received the subject PAN. Thus, the burden of proving its actual receipt of the PAN lies with Respondent.

Respondent failed to prove the fact of mailing of the PAN. He never presented the Registry Receipt issued by the Bureau of Posts or the Registry Return card signed by Petitioner or its authorized representative.

Neither did Respondent present a Certification issued by the said Bureau of Posts *and* any other pertinent document executed with its intervention. The *Transmittal Letter dated December 28, 2018 issued by Philpost* cannot be considered as equivalent to the said Certification, simply because it is unsigned. As a corollary, the Court cannot also consider the same *Transmittal Letter* to represent as *"any other document executed with* [the Bureau of Posts'] *intervention"*, without the required Certification from the same Bureau.

In any case, there is no indication that the mailed letter, *i.e.*, the subject PAN, was, in fact, received by Petitioner, as the addressee thereof. Such being the case, the inevitable conclusion is that the said PAN was not received by Petitioner before the issuance and service of the subject FAN on January 13, 2017.

In this connection, Section 228 of the NIRC of 1997, as amended, provides, in part, as follows:

> "SEC. 228. *Protesting of Assessment.* — **When the Commissioner or his duly authorized representative finds that proper taxes should be assessed, he shall first notify the taxpayer of his findings**: *Provided, however*, That a pre-assessment notice shall not be required in the following cases:
>
> xxx xxx xxx

The taxpayers shall be informed in writing of the law and the facts on which the assessment is made; otherwise, the assessment shall be void.

Within a period to be prescribed by implementing rules and regulations, the taxpayer shall be required to respond to said notice. If the taxpayer fails to respond, the Commissioner or his duly authorized representative shall issue an assessment based on his findings." [62]

Section 3.1.6 of RR No. 12-99, as amended by RR No. 18-2013, provides as follows:

"SECTION 3. ***Due Process Requirement in the Issuance of a Deficiency Tax Assessment. –***

3.1 Mode of procedure in the issuance of a deficiency tax assessment:

3.1.1 *Preliminary Assessment Notice (PAN).* – If after review and evaluation by the Commissioner or his duly authorized representative, as the case may be, it is determined that there exists sufficient basis to assess the taxpayer for any deficiency tax or taxes, **the said Office shall issue to the taxpayer a Preliminary Assessment Notice (PAN) for the proposed assessment**. It shall show in detail, the facts and the law, rules and regulations, or jurisprudence on which the proposed assessment is based (see illustration in ANNEX A hereof).

If the taxpayer fails to respond within fifteen (15) days from date of receipt of the PAN, he shall be considered in default, in which case, a Formal Letter of Demand and Final Assessment Notice (FLD/FAN) shall be issued calling for payment of the taxpayer's deficiency tax liability, inclusive of the applicable penalties.

If the taxpayer, within fifteen (15) days from date of receipt of the PAN, responds that he/it disagrees with the findings of deficiency tax or taxes, an FLD/FAN shall be issued within fifteen (15) days from filing/submission of the taxpayer's

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62 *Emphasis supplied.*

response, calling for payment of the taxpayer's deficiency tax liability, inclusive of the applicable penalties."[63]

Based on the foregoing provisions, part of the due process requirement in the issuance of a deficiency tax assessment is the issuance and service of the PAN. Moreover, Petitioner is given fifteen (15) days from receipt of the PAN within which to respond thereto, before the issuance of the FLD and FAN by the BIR.

In *Commissioner of Internal Revenue vs. Metro Star Superama, Inc.*,[64] the Supreme Court held:

> "...**it is clear that the sending of a PAN to taxpayer to inform him of the assessment made is but part of the 'due process requirement in the issuance of a deficiency tax assessment,' the absence of which renders nugatory any assessment made by the tax authorities**. The use of the word '*shall*' in subsection 3.1.2 describes the mandatory nature of the service of a PAN. The persuasiveness of the right to due process reaches both substantial and procedural rights and the failure of the CIR to strictly comply with the requirements laid down by law and its own rules is a denial of Metro Star's right to due process. **Thus, for its failure to send the PAN stating the facts and the law on which the assessment was made as required by Section 228 of R.A. No. 8424, the assessment made by the CIR is void**."[65]

Apropos, tax assessments issued in violation of the due process rights of a taxpayer are null and void.[66]

Thus, for failure of Respondent to prove the sending of the subject PAN, which is part of the due process requirement in the issuance of a deficiency tax assessment, the subject tax assessments are void.

Finding that the subject tax assessments are void on the above-stated two (2) grounds, *i.e.*, for lack of authority of the ROs to examine Petitioner and for violation of the latter's right to due process, it is no longer necessary to address or resolve the other issues and arguments raised by the parties.

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63 *Emphasis supplied.*
64 G.R. No. 185371, December 08, 2010.
65 *Emphasis supplied.*
66 Commissioner of Internal Revenue v. Avon Products Manufacturing, Inc., et al., G.R. Nos. 201398-99, and 201418-19, October 03, 2018.

It must be emphasized that a void assessment bears no valid fruit.[67] Such being the case, the subject tax assessment cannot be enforced against Petitioner.

Petitioner is not liable to pay the subject compromise penalties.

Lastly, since the subject tax assessments are void, Petitioner cannot be held liable for the same, including the imposed compromise penalties in the total amount of Php40,000.00. Nevertheless, it must be stressed that a compromise is, by its nature, mutual in essence.[68] It implies agreement. One party cannot impose it upon the other.[69] Compromise penalties are only amounts suggested in settlement of criminal liability and may not be imposed or exacted on the taxpayer in the event of refusal to pay the suggested amount.[70] Considering that there is no indication that Petitioner consented to the subject compromise penalty, the said amount total cannot likewise be sustained.

WHEREFORE, in light of the foregoing considerations, instant *Petition for Review* is **GRANTED**. Accordingly, the assailed FAN dated January 13, 2017, holding Petitioner liable for deficiency income tax, VAT, EWT, DST, IAET, and compromise penalty, in the aggregate amount of Php5,759,540.75, for taxable year 2013, is **CANCELLED** and **SET ASIDE**. Consequently, Respondent is **ENJOINED** and **PROHIBITED** from collecting the said amount against Petitioner. Consequently, Respondent is **ENJOINED** and **PROHIBITED** from collecting the said amount against Petitioner.

SO ORDERED.

MA. BELEN M. RINGPIS-LIBAN
Associate Justice

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[67] Refer to Commissioner of Internal Revenue v. Reyes, G.R. Nos. 159694 and 163581, January 27, 2006.

[68] Refer to Vda. De San Agustin v. Commissioner of Internal Revenue, G.R. No. 138485, September 10, 2001.

[69] Commissioner of Internal Revenue v. Abad, et al., G.R. No. L-19627, June 27, 1968.

[70] Refer to Part III.4, Revenue Memorandum Order No. 7-2015.

WE CONCUR:

ERLINDA P. UY
Associate Justice

MARIA ROWENA MODESTO-SAN PEDRO
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.

ERLINDA P. UY
Associate Justice
Chairperson

CERTIFICATION

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

ROMAN G. DEL ROSARIO
Presiding Justice