

**REPUBLIC OF THE PHILIPPINES  
COURT OF TAX APPEALS  
QUEZON CITY**

***EN BANC***

**COMMISSIONER OF INTERNAL  
REVENUE,**

*Petitioner,*

**CTA EB No. 489**  
(C.T.A. CASE No. 6986)

Present:

-versus-

**Acosta, P.J.,  
Castañeda, Jr.,  
Bautista,  
Uy,  
Casanova,  
Palanca-Enriquez,  
Fabon-Victorino,  
Mindaro-Grulla, and  
Manalastas, JJ.**

**HEADSTRONG PHILIPPINES, INC.,**  
*Respondent.*

Promulgated:

**AUG 26 2010**

*Mr. Apolinario  
Gila*

X-----X

**DECISION**

**ACOSTA, PJ:**

Before this Court of Tax Appeals *En Banc*<sup>1</sup> is a Petition for Review filed on June 2, 2009 assailing the Decision of the Court of Tax Appeals Second Division<sup>2</sup> dated January 19, 2009 and the subsequent Resolution dated April 21, 2009,

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<sup>1</sup> Court *En Banc*.

<sup>2</sup> Court Second Division.

affirming the assailed Decision. The dispositive portion of the assailed Decision reads:

**"WHEREFORE**, premises considered, the Petition For Review is hereby **GRANTED**. Accordingly, Assessment Notice No. VT-14338-FY-00-03-349 dated July 18, 2003 issued against petitioner, representing its alleged deficiency value-added tax liabilities for the four quarters of the fiscal year ended March 31, 2000 in the total amount of SEVENTEEN MILLION FIVE HUNDRED EIGHTY THOUSAND SIX HUNDRED THIRTY EIGHT PESOS AND 15/100 (P17,580,638.15), inclusive of surcharges and interests, is hereby **CANCELLED** and **WITHDRAWN**.

**SO ORDERED."**

The Court Second Division found the pertinent facts<sup>3</sup> to be as follows:

Petitioner (hereinafter "Respondent") is a duly registered domestic corporation, with principal office at 15<sup>th</sup> Floor, Export Bank Plaza, Sen. Gil Puyat corner Chino Roces Avenue, Makati City. Its primary purpose as stated in Article II of its Amended Articles of Incorporation is "to carry on the business (of) making computer programs principally for the export market; to perform such programming and computer-related consultancy services; and to engage in export trading and other related consultancy services xxx. It is also duly registered with the Bureau of Internal Revenue (BIR) as evidenced by its Certificate of Registration dated September 23, 1994 and Taxpayer's Identification No. 001-008-136-000. Petitioner was formerly called James Martin & Co. – Philippines, Inc. It changed its name to Headstrong Philippines, Inc. effective September 13, 2000 as proven by the Certificate of Filing of Amended Articles of Incorporation and By-Laws issued by the Securities and Exchange Commission.

Respondent (hereinafter "Petitioner") is the official charged with the duty to assess and collect internal revenue taxes, as well as the power to cancel disputed assessments, holding office at the BIR National Office Building, Diliman, Quezon City.

For the four quarters of the fiscal year ended March 31, 2000, respondent filed its Quarterly VAT Returns on July 26, 1999 (1<sup>st</sup> Quarter), October 25, 1999 (2<sup>nd</sup> Quarter), January 27, 2000 (3<sup>rd</sup> Quarter) and April 25, 2000 (4<sup>th</sup> Quarter).

On July 24, 2003, respondent received from petitioner a Formal Letter of Demand with attached Assessment Notice No. VT-14338-FY-00-03-349 and Details of Discrepancies, all dated July 18, 2003, informing respondent of its alleged deficiency value-added taxes in the amount of P17,580,638.15, inclusive of fifty percent (50%) surcharge and interests for the fiscal year ended March 31, 2000, broken down as follows:

|                               |                      |
|-------------------------------|----------------------|
| Deficiency Value-Added Tax    |                      |
| Taxable Sales per return      | 29,785,080.00        |
| Add: Undeclared Income        | <u>39,925,520.95</u> |
| Total Sales subject to VAT    | <u>69,710,600.95</u> |
| Output tax due thereon (10%)  | 6,971,060.09         |
| Add: In tax carried over from | 10,101,776.83        |

<sup>3</sup> Rollo pp. 19-24.

|                                    |                      |                             |
|------------------------------------|----------------------|-----------------------------|
| prev. qtr                          |                      |                             |
| Add: Allowable Input tax:          |                      |                             |
| Amount claimed per tax return      | 7,698,851.40         |                             |
| Less: Unsupported input tax        | <u>2,725,820.27</u>  | 4,973,031.13                |
| Allowable VAT credit:              |                      |                             |
| Amount claimed per tax return      | 2,391,017.80         |                             |
| Less: Unsupported VAT credit       | <u>1,412,906.37</u>  | <u>978,111.43</u>           |
| Total                              |                      | 16,052,919.39               |
| Less: Input Tax carried forward    | <u>17,213,138.22</u> | <u>1,160,218.83</u>         |
| Deficiency Value-Added Tax         |                      | 8,131,278.92                |
| Add: 50% Surcharge                 |                      | <u>4,065,639.46</u>         |
| Total                              |                      | 12,196,918.38               |
| Add: Interest (4-25-00 to 8-19-03) |                      | <u>5,383,719.77</u>         |
| Total Amount Due                   |                      | <u><u>17,580,638.15</u></u> |

As admitted in the Joint Stipulation of Facts and Issues, the assessment allegedly arose from the following:

"a) Respondent allegedly failed to pay the VAT due on undeclared income amounting to P39,925,520.95. Based on the Preliminary Assessment Notice (PAN) attached to the letter of the petitioner to respondent dated February 24, 2003, the alleged undeclared income constituted income payments from the following:

|                                     |                        |
|-------------------------------------|------------------------|
| 1. Philippine Telephone Corporation | P 1,155,485.60         |
| 2. Citibank                         | 13,519,435.23          |
| 3. Social Security System           | <u>50,584,909.81</u>   |
| Total                               | P 65,259,890.64        |
| Less: SSS revenue per invoice       | <u>25,334,369.69</u>   |
|                                     | P <u>39,925,520.95</u> |

b) Respondent allegedly failed to support with VAT invoices and official receipts input taxes amounting to P2,725,820.27.

c) Respondent allegedly failed to support with Certificate of Creditable Tax Withheld at Source (BIR Form 2307) the VAT credits amounting to P1,412,906.37, which respondent claimed in its tax return. Hence, the amount was disallowed pursuant to Sec 4.114 (D) of Revenue Regulations 2-98 dated April 17, 1998 as shown below:

|                                            |                       |
|--------------------------------------------|-----------------------|
| VAT credits claimed per return             | P 2,391,017.80        |
| Less: VAT Credits supported with Form 2307 | <u>78,111.43</u>      |
| Disallowed VAT credits                     | P <u>1,412,906.37</u> |

d) Respondent's input tax of P17,213,138.22 carried forward from the previous quarters was disallowed allegedly because the "tax benefit" of this amount has already been forwarded to succeeding periods.

e) Respondent allegedly filed a false or fraudulent return with intent to evade tax, in which case the alleged applicable period of prescription for the subject assessment is ten (10) years.



f) A fifty percent (50%) surcharge has been imposed on the respondent allegedly because respondent filed a false or fraudulent return as shown by its alleged failure to report sales, receipts or income in an amount exceeding thirty percent (30%) of that declared in its return.

On August 18, 2003, respondent, through its tax counsel, SGV & Co., filed a protest requesting the withdrawal and cancellation of the said assessment. Attached to the protest letter were supporting documents such as Formal Assessment Notice and the Certificates of Creditable Tax Withheld.

Due to petitioner's inaction and before it could be barred by prescription, respondent elevated its claim before this Court through a Petition for Review on May 14, 2004.

Petitioner filed through registered mail an Answer on July 5, 2004, duly received by this Court on July 14, 2004, raising the following Special and Affirmative Defenses:

9. He reiterates and repleads the preceding paragraphs of this answer as part of his Special and Affirmative Defenses;

10. Section 228 of the Tax Code, partly provides:

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 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.

Considering the failure of petitioner to submit all relevant supporting documents within sixty (60) days from filing its protest, the assessments have already become final by operation of law.

11. Since the assessments have become final, this Honorable Court has no jurisdiction to act on the instant petition.

12. Assuming *arguendo* that this Honorable Court has jurisdiction to act on the instant petition, petitioner was assessed for deficiency VAT for the reason that petitioner failed to pay the VAT due on undeclared income amounting to P39,925,520.95 during the year, in violation of Section 108 (A) of the Tax Code.

13. Petitioner failed to substantiate with VAT invoices or official receipts on its claimed input tax in the amount of P2,725,820.27, which must be credited against its output tax due, in violation of Section 110 of the Tax Code.

14. Petitioner failed to support with Certificate of Creditable Tax Withheld at Source (BIR Form No. 2307) the VAT credits amounting to P1,412,906.37, claimed in its Income Tax return, hence, the same should be disallowed pursuant to Section 4.114 (D) of Revenue Regulations No. 2-98 dated April 17, 1998.



15. Petitioner's claimed input tax in the amount of P17,213,138.22 being carried forward to the succeeding period should be disallowed pursuant to Section 110 (B) of the Tax Code, which provides that if the input tax exceeds the output tax, the excess shall be carried over to the succeeding quarter/s.

16. Pursuant to Section 222 of the Tax Code, the BIR may assess petitioner for deficiency VAT within ten (10) years from the discovery of falsity, fraud, or omission.

17. Petitioner was subjected to 50% surcharge pursuant to Section 248 (b) of the NIRC which states that:

"In case of willful neglect to file a return within the period prescribed by this Code or Regulations..the penalty to be imposed shall be fifty percent (50%) of the tax or deficiency tax..."

18. The assessments issued against petitioner for deficiency VAT for fiscal year ended March 31, 200, covered under Assessment Notice No. VT-14338-FY-00-03-349 dated July 18, 2003, was made in accordance with existing laws and regulations.

19. All presumptions are in favor of the correctness of tax assessments.

On January 19, 2009, the CTA Second Division rendered the assailed Decision, which granted the Petition for Review and declared Assessment Notice No. VT-14338-FY-00-03-349 as cancelled and withdrawn. Petitioner filed his Motion for Reconsideration on the said Decision on February 5, 2009. The CTA Second Division, however, denied petitioner's motion in a Resolution dated April 21, 2009.

Hence, petitioner filed the instant Petition for Review before the CTA *En Banc* seeking the reconsideration of the CTA Second Division's Decision and Resolution, and praying that a judgment be rendered ordering respondent to pay the amount of P17,580,638.15 as deficiency value-added tax for fiscal year ended March 31, 2000, plus accrued 25% surcharge for late payment and 20% interest per annum from August 19, 2003 until fully paid pursuant to Section 248 and 249 of the Tax Code.

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The CTA *En Banc* promulgated a resolution on July 21, 2009 ordering the parties to file their respective memoranda.

On August 24, 2009, respondent filed its Memorandum. Petitioner, on the other hand, failed to file its Memorandum. Thereafter, the CTA *En Banc* issued a resolution on September 4, 2009 submitting the case for decision. On October 6, 2009, Petitioner filed a Manifestation with Motion to adopt all the arguments found in his Petition for Review as part of his Memorandum and to set aside the Court *En Banc's* September 4, 2009 Resolution. On October 15, 2009, the CTA *En Banc* denied the Motion but notes the manifestation that petitioner is adopting all the arguments in the Petition for Review dated May 22, 2009 as his Memorandum.

Petitioner raised the following issues in his Petition for Review:

I

Whether or not the VAT returns filed by respondent for fiscal year ended March 31, 200 were false or fraudulent returns with intent to evade tax.

II

Whether or not the right of petitioner to assess respondent for deficiency VAT for fiscal year ended March 31, 2000 has already prescribed.

III

Whether or not this Honorable Court has jurisdiction to entertain the instant case.

Petitioner primarily argues that respondent filed false or fraudulent VAT returns for fiscal year ended March 31, 2000 with intent to evade tax. Thus, respondent may be assessed for deficiency VAT within the 10-year period provided under Section 222 of the 1997 Tax Code. Likewise, petitioner additionally posits that the court in division has no jurisdiction to act on the case



at bar since the Formal Assessment Notice (FAN) for deficiency VAT issued by the BIR to respondent had already become final and demandable before it filed its petition for review before the court in division on May 24, 2004.

### THE COURT *EN BANC*'S RULING

The CTA *En Banc* finds the petition for review bereft of merit.

After a closer look and scrutiny of the arguments laid down by petitioner in the instant petition for review, the CTA *En Banc* observes that the grounds relied upon and matters raised therein are mere restatements of petitioner's previous arguments before the CTA Second Division, which have already been exhaustively considered, discussed and passed upon in the assailed Decision and Resolution. Hence, the CTA *En Banc* adheres to the factual findings of the CTA Second Division that the assessments have been issued beyond the prescriptive period provided under Section 203 of the Tax Code.

The Court *En Banc* deems it wise to resolve jointly the issue on prescription of the assessment and the existence of falsity or fraud with intent to evade tax in the filing of respondent's VAT returns as these are interrelated.

In the case at bar, Secs. 203 and 222 of the Tax Code lay down the applicable periods for the assessment and collection of taxes, *viz*:

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



prescribed by law for the filing thereof shall be considered as filed on such last day.

**SEC. 222. Exceptions as to Period of Limitation of Assessment and Collection of Taxes. —**

(a) In the 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 ten (10) years after the discovery of the falsity, fraud or omission: Provided, That in a fraud assessment which has become final and executory, the fact of fraud shall be judicially taken cognizance of in the civil or criminal action for the collection thereof.

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As the case involved a deficiency VAT assessment, the following provision of the Tax Code must likewise be taken into consideration:

**SEC. 114. Return and Payment of Value-added Tax. —**

(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.

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Following the above provisions, it is thus clear that, as a rule, the assessment and collection of taxes must be made within the three-year prescriptive period counted from the date of actual filing of the return or from the last date prescribed by law for the filing of such return, whichever comes later; the exceptions being found in Section 222 of the same Code. In the case of VAT, Sec. 114 (A) requires the taxpayer to file the return twenty-five days following the close of each taxable quarter.



As borne by the records of the case, the following dates are material:

| VAT Quarter Covered     | Date Required for Filing of Return/Date of Actual Filing | End of Three-year Prescriptive Period | Date of Issuance of Final Assessment Notice |
|-------------------------|----------------------------------------------------------|---------------------------------------|---------------------------------------------|
| 1 <sup>st</sup> Quarter | July 26, 1999                                            | July 25, 2002                         | July 18, 2003                               |
| 2 <sup>nd</sup> Quarter | October 25, 1999                                         | October 24, 2002                      | July 18, 2003                               |
| 3 <sup>rd</sup> Quarter | January 27, 2000                                         | January 26, 2003                      | July 18, 2003                               |
| 4 <sup>th</sup> Quarter | April 25, 2000                                           | April 24, 2003                        | July 18, 2003                               |

From the foregoing data, it is manifest that petitioner's right to assess respondent for deficiency VAT for fiscal year ended March 31, 2000 has already prescribed when it issued Assessment Notice No. VT-14338-FY-00-03-349.

Petitioner, however, would like this Court *En Banc* to rule that the foregoing VAT returns filed by respondent are false or fraudulent and thus, the exception under Sec. 222 of the Tax Code prescribing a longer ten-year period upon discovery of falsity or fraud shall apply. In alleging that the returns filed were false or fraudulent with intent to evade tax, petitioner merely compared the income payment as appearing in the Certificates of Creditable Tax Withheld at Source (BIR Form 2307) issued by Piltel, Citibank and SSS vis-à-vis the income of respondent per the VAT Returns and deduced therefrom that petitioner had undeclared income in the amount of P39,925,080.95.

On the other hand, respondent presented Mr. Ericson Suarez, its Accounting Staff, who testified that the alleged discrepancy between the amounts of income generated reflected in the returns was caused by the different accounting methods used. It should be reiterated that VAT on services is based on gross receipts or collections as required under the Tax Code, while for withholding tax purposes, the accrual method is used as required under Section 57 (B) of the same Code and of Revenue Regulations 2-98.

As pointed out in the assailed Decision, the adoption of the accrual method for withholding tax purposes – withholding of tax at source is reported in the period income becomes payable regardless whether it has been paid or not – and

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the case method of accounting for VAT purposes – income is reported based on gross receipts/ collection – results to a timing difference in recognition of its income,<sup>4</sup> thus causing discrepancies between the income that was reported by the petitioner against the gross income that appears in the BIR Form 2307 representing withholding made by their clients. Further, in the summary of official receipts and in the sworn statement of Mr. Suarez, petitioner was able to show that the alleged undeclared income was collected outside the fiscal year ended March 31, 2000.

In the earlier case of *Aznar vs. Court of Tax Appeals*<sup>5</sup>, the Supreme Court had the occasion to differentiate falsity (due to mistake, carelessness and ignorance) and fraud in relation to the filing of tax returns, which is:

"... The fraud contemplated by law is actual and not constructive. It must be intentional fraud, consisting of deception willfully and deliberately done or resorted to in order to induce another to give up some legal right. Negligence, whether slight or gross, is not equivalent to the fraud with intent to evade the tax contemplated by law. It must amount to intentional wrong-doing with the sole object of avoiding the tax. It necessarily follows that a mere mistake cannot be considered as fraudulent intent, and if both petitioner and respondent Commissioner of Internal Revenue committed mistakes in making entries in the returns and in the assessment, respectively, under the inventory method of determining tax liability, it would be unfair to treat the mistakes of the petitioner as tainted with fraud and those of the respondent as made in good faith."

Likewise, in the case of *Commissioner of Internal Revenue vs. Melchor Javier*<sup>6</sup>, the Supreme Court ruled that:

"Fraud is never imputed and the courts never sustain findings of fraud upon circumstances which, at most, create only suspicion and

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<sup>4</sup> *Telesat, Inc. vs. Commissioner of Internal Revenue*, CTA Case No. 6812, January 2, 2006, with Entry of Judgment dated March 17, 2006.

<sup>5</sup> G.R. No. L-20569, August 23, 1974

<sup>6</sup> G.R. No. 78953, July 31, 1991



the mere understatement of a tax is not itself proof of fraud for the purpose of tax evasion."

Clearly then, petitioner was not able to establish through the evidence presented, that respondent indeed filed a false or fraudulent return with intent to evade tax. At this point, it bears stressing that:

"Our tax laws mandates a statute of limitations in the collection of taxes for the purpose of safeguarding taxpayers from any unreasonable examination, investigation or assessment. Thus, the law on prescription, being a remedial measure, should be liberally construed in order to afford such protection. As a corollary, the exceptions to the law on prescription should perforce be strictly construed."<sup>7</sup>

Consequently, absent a showing that respondent filed false or fraudulent returns with intent to evade tax, it is clearly established that Assessment Notice No. VT-14338-FY-00-03-349 is invalid because it was issued beyond the three-year prescriptive period.<sup>8</sup>

Anent the third issue, the Court Second Division was correct in ruling that as there was no valid assessment to speak of, petitioner cannot argue that the subject Assessment Notice No. VT-14338-FY-00-03-349 has become final and executory for respondent's failure to file its appeal before this Court within thirty days after the lapse of the 180-day period provided under Sec. 228 of the Tax Code. In another case, the Supreme Court declared null and void an assessment issued beyond the prescriptive period, notwithstanding the taxpayer's failure in said case to file an administrative protest within the thirty-day period after receipt of the final assessment notices.<sup>9</sup>

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<sup>7</sup> Takasago Import-Export Corporation vs. Commissioner of Internal Revenue, CA-GR SP No. 78777, January 31, 2007.

<sup>8</sup> Philippine Journalists, Inc. vs. Commissioner of Internal Revenue G.R. No. 162852, December 16, 2004.

<sup>9</sup> *Ibid.*



In sum, the Court *En Banc* finds no cogent justification to disturb the findings and conclusion spelled out in the assailed January 19, 2009 Decision and April 21, 2009 Resolution of the CTA Second Division. What the instant petition seeks is for the Court En Banc to view and appreciate the arguments/discussions raised by the petitioner in its own perspective of things, which unfortunately had already been exhaustively considered and passed upon.

**WHEREFORE**, the instant Petition for Review is hereby **DENIED** for lack of merit. The assailed Decision dated January 19, 2009 and Resolution dated April 21, 2009 of the CTA Second Division are hereby **AFFIRMED**.

**SO ORDERED.**

  
**ERNESTO D. ACOSTA**  
Presiding Justice

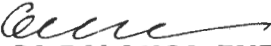
**WE CONCUR:**

  
**JUANITO C. CASTANEDA, JR.**  
Associate Justice

  
**LOVELL R. BAUTISTA**  
Associate Justice

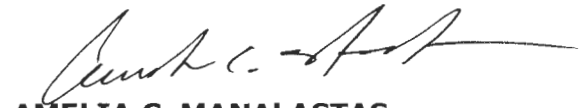
  
**ERLINDA P. UY**  
Associate Justice

  
**CAESAR A. CASANOVA**  
Associate Justice

  
**OLGA PALANCA-ENRIQUEZ**  
Associate Justice

  
**ESPERANZA R. FABON-VICTORINO**  
Associate Justice

  
**CIELITO N. MINDARO-GRULLA**  
Associate Justice

  
**AMELIA C. MANALASTAS**  
Associate Justice

**CERTIFICATION**

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

  
**ERNESTO D. ACOSTA**  
Presiding Justice