REPUBLIC OF THE PHILIPPINES
Court of Tax Appeals
QUEZON CITY

SECOND DIVISION

MAGNETIC RESONANCE IMAGING SERVICES (as represented by HOSPITAL MANAGEMENT SERVICES, INC.),
Petitioner,

- versus -

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

C.T.A. CASE NO. 6608

Members:

CASTAÑEDA, JR., *Chairperson*
UY, *and*
PALANCA-ENRIQUEZ, *JJ.*

Promulgated:
OCT 2 0 2009
11:52 a.m.

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DECISION

UY, J.:

This is a *Petition for Review* seeking the cancellation and withdrawal of the deficiency income tax assessment and deficiency expanded withholding tax assessment issued by respondent, Commissioner of Internal Revenue, against petitioner, Magnetic Resonance Imaging Services (as represented by Hospital Management Services, Inc.), for taxable year 1998 in the amounts of ₱ 10,649,555.69 and ₱ 19,410.76, respectively.

THE FACTS

Petitioner Magnetic Resonance Imaging Services was an unincorporated joint venture formed between General Electric Philippines, Inc. and Medical Center

Manila – Hospital Management Services, Inc., which existed under and by virtue of the laws of the Republic of the Philippines, with business address at the 1122 Gen. Luna Street, Paco, Manila. It was dissolved on December 31, 1998, and is herein represented by one of its partners, Medical Center Manila – Hospital Management Services, Inc.[1]

Respondent, on the other hand, is the duly appointed Commissioner of Internal Revenue, with power, among others, to decide disputed assessments of internal revenue taxes and penalties imposed in relation thereto, with office address at the Fifth Floor, Bureau of Internal Revenue (BIR) National Office Building, BIR Road, Diliman, Quezon City.[2]

On April 15, 1999, petitioner filed its Income Tax Return ("tentative return", as referred to by the parties) for the year ended December 31, 1998.[3] Subsequently, on July 15, 1999, petitioner submitted its amended Income Tax Return[4] ("final return", as referred to by the parties).

On December 19, 2001, respondent issued Formal Assessment Notice (FAN) No. 34-24-000006-98, which petitioner received on January 2, 2002, alleging that petitioner has income tax and expanded withholding tax (EWT) deficiencies for taxable year 1998, in the total amounts of ₱ 9,303,036.31 and ₱ 19,410.76, respectively, inclusive of surcharge and interest. The income tax deficiency allegedly arose from the disallowance of the following items:

a) Writedown of Property and Equipment	₱ 13,000,000
b) Hospital Medical Supplies	₱ 196,091
c) Light and Water	₱ 20,911
d) Telephone	₱ 20,911

[1] *Petition for Review*, Par. 1; *Answer*, Par. 1, Docket, pp. 1 and 40, respectively.
[2] *Petition for Review*, Par. 2; *Answer*, Par. 1, Docket, pp. 1- 2, and 40.
[3] BIR Records, pp. 342-361. See also *Transcript of Stenographic Notes (TSN)*, November 13, 2003, p. 12.
[4] *Joint Stipulation of Facts and Issues (JSFI)*, Par. 3, Docket, p. 97. BIR Records, pp. 84-96.

e) Repairs and Maintenance	₱	6,650,486
f) Miscellaneous Expense	₱	11,656
g) Insurance Expense	₱	217,929

With respect to the EWT deficiency, the same allegedly arose from the alleged failure to withhold the basic tax due of ₱ 10,260 on salaries and wages.[5]

Admittedly, FAN No. 34-24-000006-98 was based on the tentative return submitted by petitioner, instead of the final return which it filed on July 15, 1999.[6] The said FAN was duly protested by petitioner,[7] through SGV & Co., by filing an administrative protest letter dated January 31, 2002 and received by the Bureau of Internal Revenue, Revenue Region No. 6 on February 1, 2002.[8]

In the Letter dated June 14, 2002, received by petitioner on September 9, 2002, respondent stated that it could not act favorably on the protest letter filed by petitioner as *"no supporting documents was submitted to refute the said assessment as of this date,*[9] and accordingly requested for the settlement of the tax liabilities within fifteen (15) days from petitioner's receipt thereof. [10]

On September 23, 2002, petitioner, through SGV & Co., filed a request for reconsideration of the respondent's letter dated June 14, 2002, and argued that *"(t)he supporting documents needed to substantiate the protest are basically the tentative and amended ITRs of the taxpayer(s), copies of which have been furnished to the BIR."*[11]

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[5] *Petition for Review*, Par. 3, Annex "A"; *Answer*, Par. 1, Docket, pp. 2, 8-15, and 40. Exhibits "11" to "16", Docket, pp. 742-747.
[6] *JSFI*, Par. 2, Docket, p. 97.
[7] *JSFI*, Par. 1, Docket, p. 97.
[8] Exhibit "F", Docket, pp. 367-373.
[9] BIR Records, p. 176.
[10] *Petition for Review*, Par. 5; *Answer*, Par. 1, Docket, pp. 3 and 40, respectively.
[11] Exhibit "G", Docket, pp. 374- 380.

In the letter dated October 2, 2002, received by petitioner on October 22, 2002, respondent informed petitioner that the subject case would be forwarded to Revenue District No. 34 under 1st endorsement for reinvestigation.[12] Further, in the letter dated October 18, 2002, received by petitioner on October 22, 2002, Revenue District Officer (RDO), Atty. David J. Alarcon requested for the presentation of the books of accounts and accounting records to Revenue Officer (RO) Susan Garcia not later than October 28, 2002.[13] On October 28, 2002, petitioner, through SGV & Co., submitted some of the documents requested by Revenue District Officer Alarcon to Revenue Officer Susana Garcia.[14]

Subsequently, respondent revised the deficiency income tax assessment against petitioner to ₱ 10,649,555.69 (inclusive of surcharge and interest) in the letter dated January 3, 2003, received by petitioner on January 27, 2003, but reiterated the deficiency expanded withholding tax assessment.[15]

On February 26, 2003, petitioner filed the instant *Petition for Review*, with a verification and certification of non-forum shopping executed by Susan Grafilo, as Chief Accountant of Hospital Management Services, Inc.[16]

On March 24, 2003, respondent filed his *Answer* alleging the following special and affirmative defenses:

> "3. The assessment is valid and correct and the taxpayer has the burden of proof to impugn its validity (Behn Mayer & Co. Collector of Internal Revenue, 27 Phil. 647). Thus, similarly held, tax assessments by tax examiners are presumed correct made in good faith. The taxpayer has the duty to prove otherwise (Commissioner of Internal Revenue vs. Construction Resources of Asia, Inc., 145 SCRA 671); and assessment duly made by a

[12] Exhibit "H" , Docket, p. 381
[13] Exhibit "I", Docket, pp. 383-384
[14] *JSFI*, Par. 5, Docket, p. 98, See also *TSN*, August 29, 2003, pp. 6-7.
[15] Exhibit "J", Docket, p. 385.
[16] Docket, pp. 1-7

Bureau of Internal Revenue examiner and approved by his superior officers will not be disturbed (Gutierrez vs. Villegas, 8 SCRA 527).

4. The burden of proof is on the taxpayer contesting the validity or correctness of an assessment to prove not only the Commissioner of Internal Revenue is wrong but that the taxpayer is right, (Tan Guan vs. Court of Tax Appeals, et al., 19 SCRA 903); otherwise, the presumption in favor of the correctness of the tax assessment stands (Inter provincial Bus Co. vs. Collector of Internal Revenue, 98 Phil. 290; Collector of Internal Revenue vs. Bohol Land Transporation Co., 107 Phil. 967).

5. The Assessment Notice No. 34-24-00000-98 and demand letter all dated December 19, 2001 have become final, executory and demandable since the petitioner failed to file the appeal with the Court of Tax Appeals on time. Petitioner filed the appeal with the Court of Tax Appeals only on March 4, 2003 or about 6 days beyond the 30-day prescriptive period as provided under Section 228 of the 1997 Tax Code reckoned from January 27, 2003, the date the petitioner received the final decision dated January 3, 2003 on the protest (Par. 10, Petition for Review) up to February 26, 2003, the last day of the prescriptive period. Pertinent portion of Section 288 of the 1997 Tax Code provides, to wit:

> *'If the protest is denied in whole or in part, or is not acted upon within one hundred eighty (180) days from submission of documents, the taxpayer adversely affected by the decision or inaction may appeal to the Court of Tax Appeals within thirty days from receipt of the said decision, or from the lapse of the (180)-day period; otherwise, the decision shall become final, executory and demandable.' (Underline Supplied)*

6. The verification and certification of non-forum shopping in the petition for review is defective; and the case thus must, be dismissed since Susan Grafilo, as the Chief Accountant of the Manila Medical Center-Hospital Management Services, Inc. is not authorized through a board resolution:

a) by the board of directors of Manila Medical Center-Hospital Management Services, Inc, (a co-venturer) to execute the verification and certification for and in behalf of the Magnetic Resonance Imaging, the joint venture itself, or alternatively,

b) by the executive board if any, of the Magnetic Resonance Imaging (the joint venture between the General Electric Philippines, Inc. and Manila Medical Center-Hospital Management Services, Inc.) to execute the verification and certification for and in behalf of the Magnetic Resonance Imaging, the joint venture itself."[17]

[17] Docket, pp. 40-43

On June 6, 2003, respondent filed a Motion To Dismiss on three (3) grounds: (a) defective verification and certification due to lack of appropriate authority of the signatory thereof, Susan Grafilo; (b) that the right to appeal has prescribed for having been filed beyond the thirty (30) day period provided under Section 228 of the 1997 Tax Code; (c) that the assessments have become final and executory and demandable; and (d) that the Court of Tax Appeals has no jurisdiction over the case.[18]

In its Comment/Opposition thereto filed on June 26, 2003, [19] petitioner points out that Susan Grafilo was authorized by the Board of Directors of Medical Center Manila – Hospital Management Services, Inc.(MCM-HSMI) and attached thereto proof of appropriate authority of Susan Grafilo to cause the preparation and filing of the instant Petition for Review , by way of a Secretary's Certificate dated February 17, 2003[20] signed by Atty. Jharl Emory Q. Tremor, Corporate Secretary of Hospital Management Services, Inc. Further, petitioner submits that contrary to respondent's claim that the instant petition for review was filed on March 4, 2003, the same was filed on February 26, 2003 well within the prescriptive period as borne by the records of this case.

In the Resolution dated July 18, 2003,[21] the Court denied respondent's Motion to Dismiss as it found the instant petition for review timely filed by Susan Grafilo, under appropriate authority from the Board of Directors of MCM-HMSI to file the same. On September 1, 2003, counsel for respondent submitted the *BIR Records*

[18] Docket, pp. 56-61
[19] Docket, pp. 66-72
[20] Docket, p. 72
[21] Docket, pp. 73-81

pertaining to this case.[22] Thereafter, on November 11, 2003,[23] the parties submitted their Joint Stipulation of Facts and Issues.

During the hearing held on November 13, 2003, the Court ordered counsel for petitioner to submit the same authorization for Susan Grafilo from General Electric Philippines, Inc., otherwise the case will be dismissed.[24] In compliance thereto, counsel for petitioner submitted the said authorization of Susan Grafilo[25] during the hearing held on January 21, 2004. Thereafter, trial on the merits ensued.

Upon termination of the parties' presentation of evidence, they were directed by the Court in the Resolution dated August 5, 2008 to simultaneously file their respective Memorandum within thirty (30) days from receipt thereof.[26] Both parties failed to comply and this case was deemed submitted for decision in the Resolution dated October 15, 2008.[27] A Motion for Reconsideration was filed by respondent on October 23, 2008, praying that he be allowed to file his Memorandum within thirty (30) days from October 20, 2008.[28] The Court granted the motion but reduced the extension period to a non-extendible period of fifteen (15) days from receipt within which to file his memorandum.[29] On November 13, 2008, respondent filed his Memorandum.[30]

For its part, petitioner also filed a Motion for Reconsideration (with Leave of Court to Admit Attached Memorandum), praying for the admission of its attached

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[22] Docket, pp. 86-92.
[23] Docket, pp. 97-99, approved in the Resolution dated November 27, 2003, Docket, p. 101.
[24] *TSN*, November 13, 2003, pp. 14-21.
[25] Docket, p. 104. *TSN*, January 21, 2004, pp. 3-4.
[26] Docket, pp. 867-868.
[27] *Id.*, p. 869.
[28] *Id.*, pp. 871-873.
[29] Resolution dated October 27, 2008, Docket, p. 875.
[30] Docket, pp. 876-883

Memorandum on November 14, 2008.[31] The Court granted the motion on November 21, 2008 and considered this case submitted for decision as of said date.[32] Hence, this Decision.

THE ISSUES

The issues as stipulated by the parties[33] are as follows:

"1. Whether or not Final Assessment Notice No. 34-24-000006-98 is valid.

2. Whether or not the writedown of property and equipment was validly disallowed as an expense and whether such expense was claimed as in the Final Income Tax Return filed by the Petitioner.

3. Whether or not the hospital medical supplies bought were validly disallowed as an expense and whether such expense was claimed in the Final Income Tax Return filed by the Petitioner.

4. Whether or not the repairs and maintenance expense were validly disallowed as an expense and whether such expense was claimed in the Final Income Tax Return filed by the Petitioner.

5. Whether or not the insurance expense was validly disallowed as an expense and whether such expense was claimed in the Final Income Tax Return filed by the Petitioner.

6. Whether or not the salaries and wages were made the basis of the assessment was subject to expanded withholding tax.

7. Whether or not Magnetic Resonance Imaging Services, Inc. was dissolved as of December 31, 1998.

8. Whether or not Medical Center Manila – Hospital Management Services, Inc., as one of the joint venture partners of Magnetic Resonance Imaging Services, Inc. has legal personality to represent the joint venture in this Petition before the Honorable Court, the subject assessment having been served upon it."

With the exception of the first and sixth issue, the remaining stipulated issues will not be discussed herein for the following reasons: (a) the second, third, fourth

[31] Docket, pp. 884-899
[32] Docket, p. 900
[33] *JSFI*, Docket, p. 98.

and fifth issues as to whether or not the writedown of property and equipment, the hospital medical supplies, the repairs and maintenance, and the insurance, respectively, were in fact claimed in the final return, is an admitted fact in the parties' Joint Stipulation of Facts wherein it is stipulated that *"the expenses being disallowed by Respondent were not even claimed as deductions from gross income by Petitioner in its final return;"*[34] (b) the seventh issue as to whether or Magnetic Resonance Imaging Services, Inc. was dissolved as of December 31, 1998 Is admitted in paragraph 1 of the Answer;[35] and (c) the eight and last issue as to whether or not the Medical Center Manila – Hospital Management Services, Inc., has the legal personality to represent the joint venture in this Petition was duly proven as counsel for petitioner was able to show, not only an authorization to cause the preparation and filing of the instant *Petition for Review* given by Hospital Management Services, Inc., but also that of the General Electric Philippines, Inc. before trial proper in this case.

However, the Court shall look into the validity of respondent's disallowance of the aforementioned expenses, together with petitioner's claim that the collection of the assailed deficiency taxes is already barred by prescription[36] as both affect the validity of the subject assessments.

<u>Petitioner's Arguments</u>

It is petitioner's position that the collection of the subject deficiency taxes is already barred by prescription. Moreover, petitioner assails the validity of FAN No. 34-24-000006-98 on several grounds: that the issuance of the notices were allegedly

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[34] *JSFI*, Par. 2 (last sentence), Docket, p. 97.
[35] Par. 1 of the *Answer* admits par. 1 of the *Petition For Review* which in part, states the petitioner was dissolved on December 31, 1998, Docket, pp. 1 and 40).
[36] Petitioner's *Memorandum*, Pars. 30-43, Docket, pp. 891-894.

tainted with irregularities; that the assessment is without basis because it is based on a "tentative return"; and that the amendment of the return has no adverse impact on petitioner's tax liability.

As regards the issue pertaining to the validity of the disallowed expenses, petitioner argues that disallowed expenses are not in the "final return", and that the other items disallowed by respondent are justifiable deductions.

Respondent's Counter-Arguments

Respondent counter-argues that FAN No. 34-24-000006-98 has been validly issued within the three (3) year prescriptive period and the same states the law and the facts upon which the same are based; that the BIR did not have any recourse but to reiterate the assessment due to petitioner's refusal to present its accounting records for verification and validation of the adjustments made in the disallowed expenses.

In support of the foregoing arguments, respondent presented evidence to prove that the 1998 audit/investigation of petitioner's tax case was duly covered by a valid Letter of Authority and was made in due course wherein sufficient time was given to petitioner to object to the proposed pre-assessment notice and that the assessment issued by the Assessment Division was duly supported with factual and legal basis.

THE COURT'S DISCUSSIONS AND RULING

Whether or not Final Assessment Notice No. 34-24-000006-98 is valid.

Petitioner assails FAN No. 34-24-000006-98 on the basis of certain alleged irregularities relating to, and in connection with, the revalidated Letters of Authority

(LOAs) issued to the examiners of respondent;[37] and that the FAN barely passed the requirements enumerated under Section 228, that *"(n)ot only was the assessment not supported by factual findings, the FAN was likewise unsupported by the law and regulations,"*[38] and that the assessment is without basis because it is allegedly based on the so-called "tentative return" or the Income Tax Return for taxable year 1998

Alleged Irregularities in the issuance of Letters of Authority

The Court notes that the supposed irregularities were raised by petitioner only before this Court, at the judicial level, and were not mentioned in petitioner's protest letters[39] at the administrative level. Failing in this regard, petitioner is deemed to have waived its right to question the same in view of the well-entrenched rule that issues not raised below cannot be resolved on review in higher courts.[40]

As a general rule, tax assessments are presumed correct and made in good faith. The taxpayer has the duty to prove otherwise. In the absence of proof of any irregularities in the performance of duties, an assessment duly made by a BIR examiner and approved by his superior officers will not be disturbed.[41]

Assessments allegedly not supported by facts and law

With respect to petitioner's claim that the subject assessments[42] are not supported by facts and law as mandated under Section 228 of the NIRC of 1997, We find the same partly meritorious based on the following findings:

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[37] Petitioner's *Memorandum*, Pars. 44-47, Docket, p. 895.
[38] *Id.*, Par. 49, Docket, p. 895
[39] Exhibits "F" and "G", Docket, pp. 367-373, and 374-380, respectively.
[40] *Villanueva, et al. vs. Spouses Salvador*, G.R. No. 139436, January 25, 2006.
[41] *Commissioner of Internal Revenue vs. Bank of the Philippine Islands,* G.R. No. 134062, 17 April 2007; *Rizal Commercial Banking Corp. vs. Commissioner of Internal Revenue,* G.R. No. 168498, 24 April 2007.
[42] Exhibits "11" to "16", Docket, pp. 742-747.

Deficiency Income Tax Assessment: A careful scrutiny of the deficiency income tax assessment,[43] shows that the factual basis for the disallowances reflect the reason: *"unsupported",* while the law upon which these are based reflect the following: "*Disallowances (Sec. 34*) and *Compromise (Sec.254*). And on the basis thereof, petitioner was able to assail the said assessments point by point in the protest letter dated January 31, 2002 filed on its behalf by SGV and Co.[44]

For instance, the disallowance of *"Writedown of Property and Equipment"* for being *"unsupported"* pursuant to *"Sec. 34"* of the National Internal Revenue Code (NIRC) of 1997 - was assailed by petitioner on the ground that *"this item was claimed by MRI only in its tentative return, and was not claimed as a deduction at all in its final return. No item in the final returns can be related or attributed to the writedown of property and equipment."*[45] Petitioner also questioned the disallowance of *"Hospital and Medical Supplies",* on the ground that that *"(t)hese are supported by schedules in the books of the company, that the amount of P196,091.36 as shown in the assessment may be a component of the total figure claimed by MRI."*[46]

Deficiency Expanded Withholding Tax: A perusal of the assessment for deficiency expanded withholding tax in the amount ₱ 19,410.76 (inclusive of surcharge and penalties)[47] shows that it does not state the fact upon which it is based. Thus, such assessment is void and should be cancelled. As a consequence thereof, resolution of the sixth stipulated issue, as to whether or not the salaries and wages were subjected to expanded withholding tax, thus becomes unnecessary.

[43] Exhibits "14" to "16", Docket, pp. 745-747.
[44] Exhibit "F", Docket, pp.367-373.
[45] Docket, p. 371.
[46] *Id.*
[47] Exhibits "11" to "13", Docket, pp. 742-744.

Assessment allegedly without basis for being based on the "tentative return"

Petitioner contends that the assessment is without basis because it is allegedly based on the so-called "tentative return" or the Income Tax Return for taxable year 1998.[48] In other words, petitioner is of the opinion that in examining its tax records for 1998, respondent should have not looked into the said "tentative return", and should have confined himself only to petitioner's "final return".

We are not persuaded.

In ascertaining the correctness of petitioner's "final return", respondent Commissioner of Internal Revenue is not prevented from looking into petitioner's supposed "tentative return" as gleaned from the provisions of Sections 5 (A) and 6 (A) of the NIRC of 1997, the pertinent provisions of which read :

> "SEC. 5. ***Power of the Commissioner to Obtain Information, and to Summon, Examine, and Take Testimony of Persons.***— **In ascertaining the correctness of any return**, or in making a return when none has been made, **or in determining the liability of any person for any internal revenue tax,** or in collecting any such liability, or in evaluating tax compliance, the Commissioner is authorized:
>
> (A) To examine **any** book, **paper, record, or other data which may be relevant or material to such inquiry** *(Emphases supplied)*
>
> *xxx xxx xxx*
>
> **"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.

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48 Petitioner's *Memorandum*, Pars. 50-52, Docket, p. 896.

> The tax or any deficiency tax so assessed shall be paid upon notice and demand from the Commissioner or from his duly authorized representative.
>
> **Any return, statement or declaration filed in any office authorized to receive the same shall not be withdrawn**: *Provided,* That within three (3) years from the date of such filing, the same may be modified, changed, or amended: *Provided, further,* That no notice for audit or investigation of such return, statement or declaration has, in the meantime, been actually served upon the taxpayer (*Emphasis supplied).*
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> xxx xxx xxx"

Based on the foregoing, once a return has been filed, or even when a return has not been filed, the Commissioner, is empowered to authorize the examination of any taxpayer to determine whether or not the latter is liable for any unpaid or deficiency internal revenue tax/es. In conducting the examination, respondent or his duly authorized representative, is given much latitude as to what documents may be examined considering that the law allows him or his authorized representative to look into "*any book, paper, record, or other data"* which may be relevant to ascertain the correctness of the return filed.

And although a return may be modified, changed, or amended, within three (3) years from the date of the filing of a taxpayer's return, as long as no notice for audit or investigation of such return, statement or declaration has, in the meantime, been actually served upon the taxpayer, the withdrawal of any previously filed return is definitely not allowed under Paragraph 3 of Section 6 of the NIRC of 1997, which states: *Any return, statement or declaration filed in any office authorized to receive the same shall not be withdrawn.*" This goes to mean that once a return has been filed, the Commissioner or his duly authorized representative, is not precluded from examining the correctness of any return filed at their office.

Moreover, the law states "any return" which is indicative that it definitely includes not only a "final return", but also a "tentative return".

<u>Whether the espenses for writedown of property and equipment, hospital medical supplies, repairs and maintenance, and insurance were validly disallowed.</u>

The first expense on the list of expenses of petitioner is the writedown of property and equipment. Petitioner stresses that this expense was claimed in the "tentative return" of petitioner but was never reflected in its unaudited financial statements for taxable year 1998, and that the same was no longer claimed in its "final return". Petitioner heavily relies on the argument that the writedown of property and equipment was no longer included in the "final return", and is trying to fairly convince this Court that respondent, as above observed, should have solely looked into the said "final return".

Inasmuch as We want to be convinced with such argument, We cannot overlook the fact that petitioner failed to explain, at the administrative level[49], the difference between the "tentative return" with its corresponding unaudited financial statements, which *"were prepared from* (petitioner's) *books with certain adjustments"*,[50] and "final return" with its audited financial statements, especially insofar as the writedown of property and equipment is concerned.

The Court notes that during trial, petitioner's witness, Susan Grafilo, explained the reason why said writedown of property and equipment was no longer reflected in the "final return". She testified and said:

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[49] Refer to BIR Records, pp. 15, 67 and 182.
[50] Exhibit "FFFFF-15", Docket, p. 836.

"Q: What was the reason why said writedown of property and equipment is no longer reflected in the amended income tax return?

A: Writedown of property and equipment is no longer reflected and should not have been reflected in the income tax return of MRI for the reason that there has been a decision to retain the value of the Magnetic Resonance Equipment which forms almost the whole of the value as stated in its books for 1997 and in 1999. Secondly, the property and equipment was already previously subject of a writedown for the taxable year of 1997 as can be shown in the Income Tax Return for 1997 and the Financial Statements filed with the Securities and Exchange Commission which makes it improbable to have another writedown in the immediately succeeding year. Lastly, MRI has not complied with any of the requirements or applied for a writedown of property and equipment for the year 1998"[51]

However, We find the foregoing explanation insufficient, as it represents only one side of the coin. It is observed that the said difference is very significant, manifested by the following major adjustments in the financial statements, among others:

1. The increase of the *Advances from Hospital Management Services, Inc.*, a liability account, from ₱ 12,587,370 to ₱ 25,000,000;[52]
2. The decrease of *REVENUES-Others* from ₱ 18,974,672 to ₱ 10,023;[53] and
3. The result of operation, from a net *income* of ₱ 10,600,309 to a net *loss* of ₱ 7,236,299.[54]

Needless to state, adjustments of this magnitude (the writedown of property and equipment in the amount of ₱ 13,000,000.00 no longer claimed in the "final return") which remain unexplained cannot overturn the findings of the examiners who conducted the audit and examination of petitioner's books of accounts, who are accorded the presumption of regularity in the performance of their official functions

[51] Exhibit "EEEE", Docket, pp. 241-242.
[52] Exhibits "FFFFF-16" and "GGGGG-5", Docket, pp. 837 and 846.
[53] Exhibits "FFFFF-17" and "GGGGG-6", Docket, pp. 838 and 847.
[54] *Id.*

in their favor. And as a logical outgrowth of this presumption of validity of assessments, when such assessments are assailed, the burden of proof is upon the complaining party (petitioner). It is incumbent upon the latter to clearly show that the assessment was erroneous, in order to relieve himself from it.[55]

In the same vein, as cases filed before this Court are litigated *de novo*, party-litigants must prove *every minute aspect* of their cases.[56] In the instant case, petitioner failed to satisfactorily explain the above-stated adjustments, and thus, We find no reason to disturb the findings of respondent in disallowing the writedown of property and equipment. This significant omission on the part of petitioner cannot be rewarded with undeserved leniency.

Anent the other disallowed expenses, Section 34(A) of the NIRC of 1997 provides as follows:

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

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[55] 51 Am. Jur. 620-621; *Interprovincial Autobus Co., Inc. vs. Collector of Internal Revenue*, 98 Phil. 290, 52 Off. Gaz. [2] 791; *Collector of Internal Revenue vs. Bohol Land Transportation Co.*, G.R. Nos. L-13099 and L-13462, 29 April 1960; *Commissioner of Internal Revenue vs. Construction Resources of Asia, et al.*, G.R. No. L-68230, 25 November 1986.

[56] *Dizon vs. Court of Tax Appeals, et al.*, G.R. No. 140944, April 30, 2008; *Atlas Consolidated Mining and Development Corporation vs. Commissioner of Internal Revenue*, G.R. No. 145526, March 16, 2007; and *Commissioner of Internal Revenue vs. Manila Mining Corporation*, G.R. No. 153204, August 31, 2005.

xxx xxx xxx

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

xxx xxx xxx." (*Emphasis supplied*)

Based on the foregoing provision, petitioner is duty bound to substantiate with sufficient evidence, all its ordinary and necessary expenses that were claimed as deductions from its gross income for the year under consideration, not only the amount thereof, but also the direct connection or relation of the same, to the development, management, operation and/or conduct of respondent's trade, business or profession. The evidence admitted by this Court, consisting of vouchers of petitioner,[57] were carefully perused. While these evidence establish the amounts of the expenses deducted, these did not, in any way, substantiate the direct connection or relation of the said expenses to the development, management, operation and/or conduct of the trade or business of petitioner.

Clearly, there is non-compliance with the substantiation requirements laid down by Section 34(A)(1)(b) of the NIRC of 1997. Therefore, the Court cannot do otherwise but uphold the deficiency income tax assessment in its entirety.

However, the corresponding compromise penalty imposed by respondent in the amount of ₱ 25,000.00, should be cancelled. Compromise penalties are amounts suggested only in the settlement of criminal liability, and may not be

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[57] Exhibits "N" to "MMM", "EEEE" to "HHHH", and "JJJJ" to "RRRR", Docket, see pp. 414-550, 595-604, and 608-625.

imposed or exacted on the taxpayer in the event that a taxpayer refuses to pay the same.[58]

In other words, compromise penalties imply mutual agreement between the taxpayer, on one hand, and the Commissioner of Internal Revenue, on the other. Thus, considering that there is no indication that petitioner is willing to pay the said amount, the same should not be imposed.

<u>Whether the collection of the deficiency taxes is already barred by prescription.</u>

Petitioner made the following arguments on the issue of prescription, to wit:

> *"37. xxx. Respondent's failure in moving for the collection of the assessed tax resulted in the prescription of the government's right to collect the deficiency.*
>
> *xxx xxx xxx*
>
> *40. Records show that assessment notice and demand letter dated 19 December 2001 were issued and sent to Administrative Section on the same date, thus collection should have been initiated on or before 19 December 2006. Hence, as period provided under Section 203 of the 1977 NIRC has prescribed, Petitioner is no longer liable to pay either the deficiency income tax or the deficiency expanded withholding tax for taxable year 1998.*
>
> *41. In addition, by Respondent's own admission, the Assessment Notice has become final on 23 February 2003, however as of the even date there was no Warrant of Distraint and/or Levy served on the respondents nor any judicial proceedings initiated by the BIR to collect the tax due based on this assessment the CIR is now proscribed from collecting the assessed tax."*[59]

These arguments are untenable.

While it has been held that when the BIR validly issues an assessment, within either the three-year or ten-year period under Section 203[60] and 222[61] of the NIRC of

[58] Revenue Memorandum Order No. 1-90.

[59] Petitioner's *Memorandum*, Docket, pp. 893-894.

[60] SEC. 203. *Period of Limitation Upon Assessment* .— 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,

1997, respectively, whichever is appropriate, it has another five (5) years after the assessment within which to collect the national internal revenue tax due thereon by distraint, levy and/or court proceeding,[62] the counting of the said five-year prescriptive period may be suspended under certain conditions. In this particular case, such period was suspended when petitioner filed the instant *Petition for Review*.

It must be recalled that Section 223 of the NIRC of 1997 provides:

> "SEC. 223. *Suspension of Running of Statute of Limitations.* — **The running of the Statute of Limitations provided in Sections 203 and 222 on** the making of assessment and **the beginning of distraint or levy or a proceeding in court for collection, in respect of any deficiency, shall be suspended for the period during which the Commissioner is prohibited from** making the assessment or **beginning distraint or levy or a proceeding in court and for sixty (60) days thereafter**, when the taxpayer requests for a reconsideration which is granted by the Commissioner; when the taxpayer cannot be located in the address given by him in the return filed upon which a tax is being assessed or collected: *Provided,* That, if the taxpayer informs the Commissioner of any change in address, the running of the Statute of Limitations will not be suspended; when the warrant of distraint

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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.

[61] 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 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.

(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 subsequent written agreement made before the expiration of the period previously agreed upon.

(c) Any internal revenue tax which has been assessed within the period of limitation as prescribed in paragraph (a) hereof may be collected by distraint or levy or by a proceeding in court within five (5) years following the assessment of the tax.

(d) Any internal revenue tax, which has been assessed within the period agreed upon as provided in paragraph (b) hereinabove, may be collected by distraint or levy or by a proceeding in court within the period agreed upon in writing before the expiration of the five (5)-year period. The period so agreed upon may be extended by subsequent written agreements made before the expiration of the period previously agreed upon.

[62] *Bank of the Philippine Islands vs. Commissioner of Internal Revenue*, G.R. No. 139736, October 17, 2005.

or levy is duly served upon the taxpayer, his authorized representative, or a member of his household with sufficient discretion, and no property could be located; and when the taxpayer is out of the Philippines." *(Emphases supplied)*

In *Republic of the Philippines vs. Ker & Company, Ltd.*,[63] the High Court explained:

"Ker & Co., Ltd. impresses upon Us that since the Republic of the Philippines filed the complaint for the collection of the deficiency income tax for the years 1948, 1949 and 1950 only on March 27, 1962, or nine years, one month and eleven days from February 16, 1953, the date the tax was assessed, the right to collect the same has prescribed pursuant to Section 332(c) of the Tax Code. The Republic of the Philippines however contends that the running of the prescriptive period was interrupted by the filing of the taxpayer's petition for review in the Court of Tax Appeals on March 1, 1956.

If the period during which the case was pending in the Court of Tax Appeals and in the Supreme Court were not counted in reckoning the prescriptive period, less than five years would have elapsed, hence, the right to collect the tax has not prescribed.

The taxpayer counters that the filing of the petition for review in the Court of Tax Appeals could not have stopped the running of the prescriptive period to collect because said court did not have jurisdiction over the case, the appeal having been interposed beyond the 30-day period set forth in Section 11 of Republic Act 1125. Precisely, it adds, the Tax Court dismissed the appeal for lack of jurisdiction and said dismissal was affirmed by the Supreme Court in L-12396 aforementioned.

Under Section 333 of the Tax Code (*now Section 223 of the NIRC of 1997)*, quoted hereunder:

> "SEC. 333. Suspension of running of statute. — The running of the statute of limitations provided in section 331 or three hundred thirty-two on the making of assessments and the beginning of distraint or levy or a proceeding in court for collection, in respect of any deficiency, shall be suspended for the period during which the Collector of Internal Revenue is prohibited from making the assessment or beginning distraint or levy or a proceeding in court, and for sixty days thereafter."

(T)he running of the prescriptive period to collect the tax shall be suspended for the period during which the Commissioner of Internal Revenue

[63] G.R. No. L-21609, September 29, 1966.

> is prohibited from beginning a distraint and levy or instituting a proceeding in court, and for sixty days thereafter.
>
> Did the pendency of the taxpayer's appeal in the Court of Tax Appeals and in the Supreme Court have the effect of legally preventing the Commissioner of Internal Revenue from instituting an action in the Court of First Instance for the collection of the tax? **Our view is that it did.**
>
> **From March 1, 1956 when Ker & Co., Ltd. filed a petition for review in the Court of Tax Appeals contesting the legality of the assessments in question, until the termination of its appeal in the Supreme Court, the Commissioner of Internal Revenue was prevented**, as recognized in this Court's ruling in *Ledesma, et al. vs. Court of Tax Appeals*,[64] **from filing an ordinary action in the Court of First Instance to collect the tax. Besides, to do so would be to violate the judicial policy of avoiding multiplicity of suits and the rule on *lis pendens.***
>
> xxx xxx xxx
>
> Thus, did the taxpayer produce the effect of temporarily staying the hands of the Commissioner of Internal Revenue simply through a choice of remedy. And, **if We were to sustain the taxpayer's stand, We would be encouraging taxpayers to delay the payment of taxes in the hope of ultimately avoiding the same**.
>
> Under the circumstances, the Commissioner of Internal Revenue was in effect prohibited from collecting the tax in question. This being so, the provisions of Section 333 of the Tax Code will apply." *(Emphasis supplied)*

In the instant case, computing from the date of issuance of the assailed assessment (FAN No. 34-24-000006-98) on December 19, 2001, to the filing of the instant Petition for Review on February 26, 2003, only two (2) years, two (2) months, and seven (7) days have elapsed due to the said suspension of the statute of limitation under Section 223 of the NIRC of 1997. This being the case, it cannot be validly argued that the collection of the assessed tax has already prescribed.

WHEREFORE, all the foregoing considered, the instant petition is **PARTIALLY GRANTED.** The deficiency expanded withholding tax assessment in the amount of ₱ 19,410.76, inclusive of surcharges and penalties, and the

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[64] 102 Phil. 931.

compromise penalty pertaining to the deficiency income tax assessment in the amount of ₱ 25,000.00, both for taxable year 1998, are hereby **CANCELLED** and **WITHDRAWN**.

However, petitioner is **ORDERED TO PAY** the respondent deficiency income tax in the amount of ₱ 9,278,036.31 for taxable year 1998, including twenty percent (20%) delinquency interest from December 19, 2001 until fully paid, pursuant to Section 249 of the NIRC of 1997.

SO ORDERED.

ERLINDA P. UY
Associate Justice

WE CONCUR:

JUANITO C. CASTAÑEDA, JR.
Associate Justice

OLGA PALANCA-ENRIQUEZ
Associate Justice

ATTESTATION

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

JUANITO C. CASTAÑEDA, JR.
Associate Justice Chairperson

CERTIFICATION

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

ERNESTO D. ACOSTA
Presiding Justice