REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

INDUSTRIAL TEXTILE MANUFACTURING COMPANY OF THE PHILIPPINES, INC.,
Petitioner,

- versus -

C.T.A. CASE NO. 4885

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:
AUG 22 1996

x - x

DECISION

This is an appeal from the decision of respondent Commissioner of Internal Revenue reiterating the judgment of deficiency income, expanded withholding, sales and documentary stamp tax for the taxable years 1980 and 1983, the details of which are enumerated hereunder:

1980 Deficiency Income Tax

Net Income per return	P 3,129,097.61
Add: Unallowable deductions: Management fee (not subjected to EWT)	713,235.00
Net income per investigation	P 3,842,332.61
Income Tax due thereon	P 1,526,933.00
Less: Income tax already assessed	1,241,639.00
Balance	P 285,294.00
Add: 20% interest from 4/16/81 to 4/15/84	171,176.40
TOTAL AMOUNT DUE AND COLLECTIBLE	P 456,470.40

1980 Deficiency Expanded Withholding Tax

Management fee not subjected to EWT		P 713,235.00
Multiply by rate of tax		x 5%
Expanded withholding tax due thereon		P 35,661.75
Add: 25% surcharge		8,915.43
14% interest from 2/1/81 to 10/18/85		23,529.62
TOTAL AMOUNT DUE AND COLLECTIBLE		P 68,106.80

1980 Deficiency Sales Tax

Taxable sales per return		P71,632,469.31
Multiply by rate of tax		x 10%
Sales tax due thereon		P 7,163,246.93
Less: Allowable tax credit	P 3,759,479.98	
Quarterly payments	2,668,559.39	6,428,039.37
Balance		P 735,207.56
Add: 25% surcharge		183,801.89
20% interest from 2/21/81 to 10/18/85		850,910.85
TOTAL AMOUNT DUE AND COLLECTIBLE		P 1,769,920.30

1980 Deficiency Documentary Stamp Tax

Increase in outstanding capital stock:

1. Class A Shares:		
Balance, December 31, 1980 -	P15,132,531.00	
Balance, January 1, 1980 -	10,036,731.00	
Increase in 1980		P 5,095,800.00
2. Class B Shares:		
Balance, December 31, 1980 -	7,872,534.00	
Balance, January 1, 1980 -	5,189,800.00	
Increase in 1980		P 2,682,734.00
Total Increase in Outstanding Capital Stock - 1980		P 7,778,534.00

Documentary stamp tax due thereon:

$$\frac{P\ 7{,}778{,}534.00}{P200.00} \times P38{,}893.00 \times P1.10 = P\ 42{,}782.30$$

Less: Amount of documentary stamp tax paid	42,221.75
Deficiency Documentary Stamp Tax	P 560.55

1983 Deficiency Sales Tax

Net taxable sales per investigation		P73,605,120.63
10% Sales tax due thereon		P 7,360,512.06
Less: Allowable tax credit per investigation		3,599,021.16
Net sales tax due		P 3,761,490.90
Less: Quarterly payments	P 2,158,094.29	
Tax credit application	310,122.02	2,478,216.31
Deficiency sales tax		P 1,283,274.59
Add: 25% Surcharge		320,818.65
Sub-total		P 1,604,093.24
Add: 20% interest from 2/1/84 to 1/16/89		1,572,636.97
TOTAL AMOUNT DUE AND COLLECTIBLE		P 3,176,730.21

1983 Deficiency Expanded Withholding Tax

Expd. withholding tax on professional fees	P 31,292.38
Expd. withholding tax on security agency fees and administrative expenses	313.90
Total expd. withholding taxes due	31,606.28
Add: 25% Surcharge	7,901.57
20% interest p/a from 2/1/84 to 1/16/89	30,986.48
TOTAL AMOUNT DUE AND COLLECTIBLE	P 70,494.33

Petitioner was a domestic corporation that was organized and existed under and by virtue of the laws of the Philippines. It was engaged in the business of manufacturing plastic jute bags and was registered with the Board of Investments as a preferred non-pioneer enterprise. At the present time, petitioner's corporate existence has already been dissolved upon approval by the Securities and Exchange Commission.

No concrete facts can be narrated from this case because apart from the figures contained in the assessments concerned, both parties have different versions of the circumstances leading up to this petition.

Petitioner alleges the following:

That on January 3, 1986, petitioner received assessment notices for deficiency income, expanded withholding, sales and documentary stamp tax for the taxable year 1980;

That petitioner filed its protest on the 1980 deficiency assessment in letters, dated January 30, 1986, and April 18, 1988, and received by respondent's representatives on January 30, 1986 and April 19, 1988, respectively;

That respondent did not act on the protest but instead issued a Warrant of Garnishment against petitioner, dated October 26, 1989;

That respondent's right to collect the alleged tax liabilities for its 1980 tax deficiencies has already prescribed after three years following the assessment of the taxes;

That the tax assessment for its 1983 tax deficiencies supposedly sent to petitioner was never received by the petitioner and that there is absolutely nothing in the BIR records to prove that said notices were sent by mail or by personal service to petitioner. What petitioner received as notice of the alleged tax deficiencies was the Warrant of Distraint and/or Levy and the Warrant of Garnishment issued against petitioner's bank, dated May 23, 1990.

From the foregoing allegations, respondent denies receiving a copy of the protest letter allegedly filed by petitioner with respect to the 1980 tax assessment. She insists that said letter protest cannot be located in the BIR records of this case. Moreover, respondent takes issue with the supposed copy of the protest letter submitted by petitioner as Exhibit "C", because such letter was unsigned thereby relegating its status to a mere scrap of paper. Respondent contends that the 1980 tax assessments issued against petitioner has become final, executory and demandable because of petitioner's failure to file a protest within the time prescribed by law.

Respondent goes further to dispute the allegations of petitioner with regard to its 1983 tax deficiencies as she insists that said assessment notice was duly issued and sent to petitioner on January 16, 1989. Thus, it is respondent's belief that the 1983 tax assessment has likewise become final, executory and demandable because no protest was ever filed thereon.

The denials of both parties as above-narrated suggest a need to tackle this particular dispute before the merits of the assessments issued can be properly disposed of.

Petitioner contends that respondent's right to collect its 1980 tax deficiencies had already prescribed the reason being that the assessment notices for its 1980 tax deficiencies were all dated October 18, 1985, so that it follows that since Batas Pambansa Blg. 700 which reduced the period of assessment and collection from five years to three years took effect in 1984, the period to collect was also shortened to three years. Moreover, since the warrant of garnishment was issued only on May 22, 1989 or three years, seven months and 4 days following the date of the assessment, the right to collect had already prescribed.

Petitioner's contention has no merit.

Revenue Memorandum Circular No. 33-84 which was issued to clarify the amendments set forth by B.P. 700 provides the following:

> "Assessments made on or after April 5, 1984 (date of approval of BP 700) will still be governed by the original five-year period if the taxes assessed thereby cover taxable years prior to January 1, 1984. Corrollarily, assessments made before April 5, 1984 shall still be governed by the original five-year period.
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> xxx xxx xxx
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> As regards collection, the institution of collection remedies either by judicial action or distraint or levy, if begun on or after April 5, 1984 shall still be governed by the five-year period if the taxes being collected are for taxable years prior to January 1, 1984. The collection of the three-year period shall apply to the collection of taxes for taxable years beginning January 1, 1984."

It is clear from the foregoing that the taxable year is the determining factor in applying the five year or three-year period, as the case maybe, thus it does not matter if the assessments were dated after the effectivity of Batas Pambansa Blg. 700. In the instant case, the taxable year subject of the assessment is 1980, so the period to collect the tax deficiencies contained therein is still five (5) years and not three (3) years as declared in BP 700. Therefore, the government's right to collect petitioner's 1980 tax deficiencies has not yet prescribed.

The contention of respondent that no protest was filed by petitioner on the 1980 assessment is contradicted by the records of this case. Petitioner presented as Exhibit "C", a copy of the protest letter, dated January 30, 1986, with a BIR stamp evidencing receipt on that same date. Respondent's assertion that no copy of such protest letter can be found in the BIR records does not necessarily mean that no protest was filed because of the fact that the BIR received the same as evidenced by its rubber stamp. Moreover, the fact that the protest was left unsigned does not reduce it to a mere scrap of paper because a cursory examination of the contents of the protest reveals a detailed rebuttal of the 1980 tax assessment setting forth the legal and factual grounds as basis of its protest with the declaration that it was made in behalf of petitioner. Therefore, the fact that counsel failed to sign the same becomes a minor and inconsequential issue insufficient to negate its existence and validity. Furthermore, petitioner's counsel, Demosthenes Gadioma, in a later correspondence with the BIR acknowledged having made the protest in a signed letter, dated April 18, 1988, which was received by respondent on April 19, 1988 (page 224, BIR records, folder II), thus confirming the protest letter at issue.

As to the 1983 tax assessment, petitioner denies receipt thereof and claims that it came to know only of its alleged 1983 tax deficiencies by means of the warrants of garnishment issued by respondent, dated May 23, 1990. Petitioner voiced its opposition to this warrant in several letters sent to respondent, dated June 1, 1990, June 14, 1990, September 13, 1990 and October 5, 1990.

Respondent, in order to prove the existence of the 1983 assessment, offered as evidence, copies of the assessment letter for 1983 (Exhibits "2", "2-a"). The BIR records submitted also revealed a certified true copy of the postal registry receipt No. 71-A (pp. 282 and 284, BIR records, folder I). However, respondent did not present any evidence that such assessment was received by the petitioner. The registry return card was not presented. Similarly, no copy of the acknowledgment receipt issued by the post office can be found in the BIR records. Well-settled is the rule that if the addressee of the letter denies receipt, the burden of proving the same shifts to the sender, thus:

> "As correctly observed by the respondent Court in its appealed decision, while the contention of petitioner is correct that a mailed letter is deemed received by the addressee in the ordinary course of mail, still, this is merely a disputable presumption; subject to controversion, and a direct denial of the receipt thereof shifts the burden upon the party favored by the presumption to prove that the mailed letter was indeed received by the addressee." **(Republic of the Philippines vs. Court of Appeals and Nielson and Company,** 149 SCRA 351)

The aforequoted ruling was utilized by this Court in disposing of a similar issue in the case entitled **Arnoldus Woodworks Inc. vs. CIR,** CTA Case No. 4269, March 18, 1994, thus:

> "Although the evidence pertaining to the case at bar reveals that the assessment notices were sent by registered mail on July 31, 1986, in the plant of petitioner in Marilao, Bulacan there is a complete absence of proof to establish that the petitioner actually received them. The respondent clings to the presumption of law that "a letter duly directed and mailed was received in the regular course of the mail". [Sec. 3(v), Rule 131 of the Revised Rules of Court].
>
> While it may be true that a letter would likely be received after more than one year from the time it was duly mailed, the respondent failed to realize that such contention is merely a disputable presumption. It is put on inference provided for by law to be conveniently used in appreciation of evidence. As such, it is subject to rebuttal which will shift the burden of proof to the party alleging the same.
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> xxx xxx xxx
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> It was therefore incumbent upon the respondent to prove by contrary evidence that the petitioner indeed received the assessment

in the due course of mail for Us to consider the present action as having been filed out of time. The *onus probandi* was shifted to respondent.

In this case, respondent's failure to prove that the assessment letter for 1983 was received by the petitioner puts the enforceability of such assessment in jeopardy. It appearing that the person liable for the payment of the tax did not receive the assessment, the assessment could not become final and executory (**Republic vs. Dela Rama**, 18 SCRA 861). The failure of the respondent to prove receipt of the assessment, by the petitioner leads to the conclusion that no assessment was issued for petitioner's 1983 alleged tax deficiencies. Consequently the government's right to issue an assessment for the said period has already prescribed. Section 318 of the 1983 Tax Code provides, thus:

> Section 318. ***Period of Limitations upon assessment and collection.*** - Except as provided in the succeeding section, internal revenue taxes shall be assessed within five years after the return was filed, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period. For the purpose 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: Provided, that the limitation shall not apply to cases already investigated prior to the approval of this Code.

This Court believes that the 1983 tax assessment allegedly issued by respondent has no force and effect and hence must be cancelled as it was not duly proven by respondent that the petitioner received the same in the face of an outright denial made by the latter.

From the foregoing, we are now left with the responsibility of disposing of the merits of the other assessment issued, specifically for taxable year 1980.

ASSESSMENT FOR DEFICIENCY INCOME TAX (1980)

Respondent assessed petitioner for deficiency income tax in the amount of P456,470.40 which stemmed from the disallowed deduction corresponding to the management fee it paid to Anscor in the amount of P713,235.00. The reason for this disallowance is the fact that petitioner failed to withhold the income tax on said amount in violation of Revenue Regulations No. 13-78 and 6-79.

Petitioner admits that it did not withhold the income tax from the management fees it paid to Anscor. However, this fact did not prevent them from including this fee as a deduction from their gross income citing Revenue Memorandum Order No. 38-83, dated November 14, 1983, which has softened the harshness of Revenue Regulation No. 13-78 when it allows the deduction of said items in case of failure to withhold the same as long as it is shown that the payee of the amount actually made the correspondent declaration in its ITR and paid the tax. To bolster its claim, petitioner presented the 1980 income tax return of Anscor (payee) filed on April 15, 1981 to prove that the management fees it received from petitioner was duly reported and paid by said payee (Exhibit "B", "B-1", "B-2").

Revenue Regulation No. 13-78 made effective and applicable to income payments made beginning November 1, 1978, provides the requirement for deductibility of such income payments, thus:

> Sec. 9, ***Requirement of deductibility.*** - Any income payment, which is otherwise deductible under Sections 30 and 57 of the Tax Code, as amended, shall be allowed as deduction from the payor's gross income only if it is shown that the tax required to be withheld has been paid to the Bureau of Internal Revenue in accordance with Sections 53, 54, 91 and 93 also of the Tax Code. *Provided,* that this additional requirement shall apply only to payment made on or after the date of the effectivity of these Regulations.

Admittedly, petitioner did not withhold the tax as required and relied mainly on Revenue Memorandum Order No. 38-83 claiming that this order allows deduction of said items in case of failure to withhold as long as the payee reported/paid the income tax due thereon. Conveniently, petitioner did not present a copy of RMO No. 38-83 nor did it quote any pertinent portions of said order to substantiate its claim. A careful reading of this Revenue Memorandum Order, however, seems to contradict petitioner's claim. RMO 38-83 provides the following guidelines:

3. <u>Guidelines For Applying Section 30(1)</u>

3.1 An amount claimed as deduction on which a tax is supposed to have been withheld under Sections 54 and 93 shall be allowed if in the course of his audit and/or investigation, the examiner discovers that:

3.1/1 No withholding of creditable or final tax was made but the payee reported the income and the withholding agent/taxpayer pays during the original audit and investigation the surcharges, interest and penalties incident to the failure to withhold the tax.

3.1/2 No withholding of creditable or final tax was made and the recipient-payee failed to report the income on due date thereof, but the withholding agent pays during the original audit and investigation the amount supposed to have been withheld, inclusive of surcharges, interest and penalties incident to his failure to withhold.

3.1/3 The withholding agent erroneously under-withheld the tax but pays during the original audit and investigation the difference in the amount supposed to have been withheld, inclusive of surcharges, interest and penalties incident to such error.

3.2 Items of deductions disallowed due to non-compliance with Section 30(1), the deficiency income tax assessment for which had been issued before the effectivity of this Revenue Memorandum Order may be allowed upon payment not later than May 15, 1984 of the withholding tax required and supposed to have been withheld and/or surcharges, interest and penalties. However, no refund or credit arising from such re-allowance of a previously disallowed deduction shall be granted.

Although we submit that the payee Anscor reported the income derived from the management fee paid by the petitioner, the fact remains that petitioner, as withholding agent, did not pay the corresponding surcharges, interest and penalties pursuant to 3.1/1 of RMO 38-83 for failure to withhold the taxes. The BIR examiners did not err in disallowing the management fee as a deduction because at the time of their investigation of petitioner's income tax deficiencies, no such penalties and surcharges were paid. Clearly, the guidelines abovecited provides the requirement that the petitioner should first pay these penalties before such item can be allowed as a deduction.

The BIR examiners also assessed the petitioner the amount of P68,106.80 corresponding to the taxes it was supposed to have withheld from the management fee it paid to Anscor.

In this regard, we find that the payment of the above-mentioned amount is no longer necessary because Anscor, the payee of the management fees, already reported the same in its income tax return, thus the government is assured that taxes on this income had already been reported and paid. Nevertheless, it is still important to point out that petitioner, for its failure to fulfill its obligation as a withholding agent of the government, is liable to pay the penalties provided for in Section 8 of Revenue Regulations No. 13-78, thus:

> **Sec. 8. *Penalties.*** - Any failure to comply with the provisions of these regulations shall be subject to ad valorem and specific penalties.
>
> (a) *Surcharges for failure to render returns, and for rendering false or fraudulent returns, delinquency in payment of taxes.* - In case of any failure to make and file a return (BIR Form 1743-A) within the time prescribed herein, not due to willful neglect, there shall be added to the tax twenty-five *per centum* (25%) of the amount of such tax, except that when a return is voluntarily and without notice from the Commissioner or any other

revenue officer field after such time, and it is shown that the failure to file it was due to reasonable cause, no such addition shall be made to the tax.

In case the failure to make and file a return is due to willful neglect or in case a false or fraudulent return is willfully made, there shall be added to the tax or to the deficiency tax to be remitted, in case any payment has been made on the basis of such return before the discovery of the falsity or fraud, a surcharge of fifty *per centum* (50%) of the amount of such tax or deficiency tax.

In case the taxes deducted and withheld by the payor are not paid or remitted within the time prescribed, there shall be added a surcharge of five *per centum* (5%) on the amount of tax unpaid and interest at the rate of fourteen *per centum* (14%) (now 20%) upon the amount required to be paid and from the time the same become due until paid.

(b) *Penalties for failure to file return and for filing fraudulent returns or statements, or to pay tax.* - Any payor liable to pay or remit the tax, to make a return or to furnish the statement of income payment and taxes withheld from the payee required under these Regulations, who refuses or neglects to pay such tax, to make such returns at the time or times herein specified shall be punished by a fine of not more than two thousand pesos (P2,000.00) and by imprisonment for not more than (6) months.

Any individual or any officer of any corporation or general co-partnership required by law to make, render, sign, and verify any return, who makes any false or fraudulent statement with intent to defeat or evade withholding under these regulations, shall be punished by a fine of not more than five thousand pesos (P5,000.00) and imprisonment of not less than two (2) years.

If any corporation or duly registered co-partnership shall refuse or neglect to make a return at the time or times herein before specified, or shall render a false or fraudulent return, such corporation or partnership shall be liable to a fine of not exceeding twenty thousand pesos (P20,000.00). (As amended by Rev. Regs. No. 6-79). (Underscoring supplied).

In order to simplify the resolution of this Court with respect to petitioner's income tax deficiency for 1980, we hereby order petitioner to pay the corresponding penalties, the payment of which will also serve as the fulfillment of the condition for the allowance of the deduction of P713,235.00 from its gross income thereby paving the way for the cancellation of the amount of P68,106.80 and P456,470.40 as originally assessed.

DEFICIENCY DOCUMENTARY STAMP TAX (1980)

The assessment for documentary stamp tax in the amount of P560.55 is no longer being disputed as petitioner has expressed its willingness to pay the same.

DEFICIENCY SALES TAX (1980)

Petitioner opposes the deficiency sales tax assessment in the amount of P1,176,920.30 for the reason that the base used in the amount of P71,632,469.31 is inflated. It is petitioner's contention that the examiners included the sales rebates and returns granted by them pursuant to agreements made at the time of the sale. On the other hand, respondent in her Memorandum, explains that the investigation conducted revealed that the petitioner has a gross sales of P71,163,246.93 subject to a 10% sales tax of P7,163,246.95. The final amount of P1,176,920.30 was a result of the added interests and surcharges imposed.

We are inclined to uphold the assessed value of P1,176,920.30 in the absence of concrete evidence refuting the findings of the revenue examiners with respect to petitioner's sales tax deficiencies for 1980. The petitioner in its protest and petition for review dismissed this particular assessment by simply stating that the taxable base used by the examiners in computing its sales tax was inflated, without providing this Court with sufficient documentary evidence to solidify its stance. On the other hand, the BIR records submitted by the respondent contains detailed computations of petitioner's gross sales as well as the amount included as surcharge and interest (pages 61-70, BIR records, Folder II).

The revenue examiners explained the total amount of deficiency sales tax as stated above in this manner, thus:

> Investigation on its business tax case disclosed that the taxpayer is a holder of PTR C-14 as a manufacturer. Further verification disclosed that the taxpayer used more of imported materials than locally purchased materials in the manufacture of plastic jute bags. A detailed scrutiny of the local

> purchases of raw materials shows that there were separate billings of the 10% sales tax indicated in the suppliers invoices in compliance with P.D. 1358. An exhaustive computation on the availability of tax credit for the purpose of determining the correct 10% sales tax paid showed that the taxpayer is deficient in the payment of 10% percentage tax as evidenced by the detailed computation shown in the attached worksheet. The taxpayer was deficient in the amount of P735,207.56, 25% surcharge P183,801.89, interest in the amount of P907,049.93 or a total of P1,826,059.38.
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> Upon presentation of the assessment to the taxpayer, the comptroller presented to the undersigned examiner the xerox copy of a Certification of the National Grains Authority showing withholding taxes on the sale of taxpayer to NGA in the amount of P716,428.71. However, the undersigned examiner did not consider this as a creditable tax, in the absence of any ruling or regulations of the Bureau whether or not this kind of Certification can be accepted as an evidence of payment or a remittance of payment. The undersigned examiner requested the taxpayer to secure from NGA a copy of BIR Form #750 required under Rev. Reg. #21-67, but the taxpayer claimed that the attached certification is the only document being issued by NGA.

In this situation, the presumption of the correctness of the assessment prevails. The Supreme Court in the case entitled **Collector of Internal Revenue vs. Bohol Land Transportation Company**, 107 Phil. 965, declared, thus:

> "All presumptions are in favor of the correctness of tax assessments. The good faith of tax assessors and the validity of their actions are presumed. They will be presumed to have taken into consideration all the facts to which their attention was called. No presumption can be indulged that all of the

> public officials of the state in various counties who have to do with the assessment of property for taxation will knowingly mistake the duties imposed upon them by law."

WHEREFORE, in view of the foregoing, the 1983 tax assessment against petitioner for deficiency income and sales tax is hereby **CANCELLED** and respondent is **ORDERED** to **DESIST** from collecting the deficiency taxes enumerated therein.

With respect to the 1980 tax assessment against petitioner, this Court modifies the same in the following manner:

1) The 1980 assessment for deficiency income taxes in the total amount of P524,577.20 is cancelled and petitioner is hereby ordered to pay the following penalties for its failure to withhold the taxes as required by law, thus:

a) Surcharge - pursuant to Section 8(a) of Rev. Reg. No. 3-78 (P35,661.75 x 50%)	P17,830.87
b) Penalty - pursuant to Section 8(a) of Rev. Reg. No. 3-78 (P35,661.75 x 5%)	1,783.08
c) Fine imposed on a corporation pursuant to Section 8(a) of Rev. Reg. No. 3-78	20,000.00
TOTAL AMOUNT OF PENALTIES DUE	P39,613.95

2) The 1980 assessment for deficiency documentary stamp tax in the amount of P560.55 is sustained.

3) Likewise, the 1980 assessment for deficiency sales tax in the amount of P1,176,920.30 is affirmed.

SO ORDERED.

RAMON O. DE VEYRA
Associate Judge

I CONCUR:

ERNESTO D. ACOSTA
Presiding Judge

CERTIFICATION

I hereby certify that this 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 Judge
Court of Tax Appeals