REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

FIRST DIVISION

HOBBIES OF ASIA, INC., Petitioner,	CTA CASE NO. 9476
	Members:
-versus-	DEL ROSARIO, *P.J., Chairperson* FABON-VICTORINO, *and* MANAHAN, *JJ.*
COMMISSIONER OF INTERNAL REVENUE, Respondent.	Promulgated: NOV 12 2019 ; 10:48 am

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DECISION

FABON-VICTORINO, *J.:*

Before the Court is the *Petition for Review*[1] filed by Hobbies of Asia, Inc. praying for the cancellation and setting aside of the Final Decision on Disputed Assessment (FDDA) dated August 18, 2016, issued against it for alleged deficiency Income Tax (IT), Value-Added Tax (VAT), Expanded Withholding Tax (EWT), and Documentary Stamp Tax (DST) in the aggregate amount of ₱20,540,505.43, inclusive of increments, for taxable year (TY) 2011.

First, the facts.

Petitioner Hobbies of Asia, Inc. is a domestic corporation, with address at No. 8, Diosdado Macapagal, Boulevard, Barangay 76, Pasay City.[2] It is primarily engage in the business of real estate, including subdivision, partitioning, and developing real properties, the improvements and permanent structures situated or

[1] Docket, pp. 10-46.
[2] Exhibit "P-1".

attached thereon; to own, use, improve, develop, subdivide, sell, exchange, lease, and hold for investment or otherwise, real estate of all kinds, including buildings, houses, apartments and other structures.[3] It is registered with the Bureau of Internal Revenue (BIR) under Certificate of Registration No. OCN 9RC0000875303E[4] with Tax Identification Number (TIN) 240-258-579-00000.[5]

Respondent, on the other hand, is the Commissioner of the Internal Revenue (CIR), with the power to decide disputed assessments, refunds of internal revenue taxes, fees or other charges, penalties imposed in relation thereto or other matters arising under the National Internal Revenue Code (NIRC) or other laws or portions thereof administered by the Bureau of Internal Revenue (BIR). He holds office at 5th Floor, BIR Building, BIR Road, Diliman, Quezon City.

On December 5, 2012, petitioner received a Letter of Authority (LOA) No. LOA-051-2012-00000381 (SN: eLA201100013573)[6] dated November 16, 2012, issued by then Regional Director Nestor S. Valeroso of Revenue Region No. 8 – Makati City, authorizing Revenue Officer (RO) Roberto Taylo and Group Supervisor Arnaldo Rase of Revenue District Office (RDO) No. 51 – Pasay City, to examine petitioner's books of accounts and other accounting records for all internal revenue taxes for TY 2011.[7]

On May 19, 2014, the same Director Valeroso issued a Memorandum of Assignment (MOA) No. RR8-051-REA-05-014-00265[8], authorizing RO Marilyn D. Guerzon and Group Supervisor Arnaldo Rase to continue the conduct of audit of petitioner's books of accounts and other accounting records for all internal revenue taxes for TY 2011.

After her tax investigation, RO Marilyn D. Guerzon, through a Memorandum[9] sent to BIR Revenue Region No. 8 – Makati City, recommended the issuance of assessment notices against petitioner to collect the deficiency taxes due.

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[3] Exhibit "P-2".
[4] Exhibit "P-3".
[5] Paragraph 1, Admitted Facts, Joint Stipulation of Facts and Issues (JSFI), docket, p. 336.
[6] Exhibit "P-32"; Exhibit "R-2", BIR records, p. 1.
[7] Par. 2, JSFI, docket, p. 336.
[8] Exhibit "R-1", BIR records, p. 128.
[9] Exhibit "R-6", BIR records, pp. 211-212.

On December 22, 2014, petitioner received a Preliminary Assessment Notice[10] (PAN) dated December 19, 2014, with attached Details of Discrepancies, assessing it for deficiency IT, VAT, EWT and DST for TY 2011 in the total amount of ₱16,864,603.95.

On January 14, 2015, petitioner received a Formal Assessment Notice (FAN) with attached Assessment Notices[11] dated January 13, 2015, reiterating the assessment against it for deficiency IT, VAT, EWT and DST for TY 2011.

On February 12, 2015, petitioner protested the FAN in a letter[12] dated February 11, 2015 filed with Regional Director Jonas DP. Amora of Revenue Region No. 8 – Makati City.

On August 24, 2016, petitioner received the assailed FDDA[13] dated August 18, 2016 with attached Details of Discrepancies, denying its protest and finding it liable for deficiency IT, VAT, EWT and DST with penalties and interests for TY 2011,[14] broken down as follows:

Tax Type	**Amount Due**
Income Tax	₱14,077,300.33
Value-added Tax	3,644,801.07
Expanded Withholding Tax	1,575,837.41
Documentary Stamp Tax	1,242,566.62
TOTAL	**₱20,540,505.43**

Aggrieved, petitioner elevated its case before the Court on September 23, 2016 *via* the instant *Petition for Review.*

In his *Answer*[15], respondent claims that: (1) the authority of RO Marilyn D. Guerzon and Group Supervisor Arnold R. Rase to investigate the internal tax liabilities of petitioner for TY 2011 was based on a Memorandum of Assignment originating from a validly issued LOA; (2) his

[10] Exhibit "R-7", BIR records, pp. 226-229.
[11] Exhibit "P-29"; Exhibits "R-8" and "R-9", BIR records, pp. 234-237 and 258-259, respectively.
[12] Exhibit "P-30".
[13] Exhibit "P-31"; Exhibit "R-10", BIR records, pp. 269-272.
[14] Par. 3, JSFI, docket, pp. 336-337.
[15] Docket, pp. 99-105.

right to investigate petitioner's IT for TY 2011 has not prescribed; and (3) the prescriptive period to assess petitioner's VAT is ten (10) years for it allegedly committed fraud in the filing of its VAT returns in which it claimed an input VAT of P2,912,496.91, when its input tax per summary list of purchases amounted to only P1,297,454.43 for TY 2011.

After the pre-trial conference, the parties filed their *Joint Stipulation of Facts and Issues*[16] on the basis of which a *Pre-Trial Order*[17] was issued on July 10, 2017.

During the trial, petitioner presented its lone witness **Leonardo B. Dela Cruz,** who testified[18] that he has been petitioner's accountant since 2010. As such, he prepares, examines financial records, monitors and ensures petitioner's compliance with tax rules and regulations, reviews assessments issued by the BIR, and safekeeps petitioner's tax returns, BIR Certificate of Registration, other permits and reportorial requirements, correspondences and other relevant documents from the BIR. He also has access to petitioner's Certificate of Incorporation, Articles of Incorporation, and other corporate documents.

He declared that petitioner is principally engaged in the business of real estate, which includes, among others, the lease of commercial spaces.

Petitioner filed the instant case to cancel and withdraw the tax assessment for TY 2011 issued against it by respondent, for deficiency IT, VAT, EWT, and DST in the aggregate amount of ₱20,540,505.43. On January 14, 2015, petitioner received a FAN to which it protested on February 12, 2015. It was however denied in the assailed FDDA which petitioner received on August 24, 2016. Thus, on September 23, 2016, petitioner filed the instant Petition for Review.

The witness confirmed that he has read and reviewed the contents of the *Petition for Review* prepared by

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[16] Docket, pp. 336-341.
[17] Docket, pp. 343-349.
[18] Docket, pp. 128-146.

petitioner's external counsel which stated that the LOA issued and served upon petitioner expressly authorized ROs Roberto Taylo and Arnaldo Rase to examine the records and books of account of petitioner for TY 2011. However, it was not them but RO Marilyn D. Guerzon who actually conducted the tax examination pursuant to a mere Memorandum of Assignment issued in her favor.

In the same initiatory pleading, petitioner also indicated that respondent's right to assess petitioner has already prescribed as could be deduced from the date of the filing of the pertinent tax returns.

Granting that respondent requested petitioner to execute a waiver of the Defense of Prescription under the Statute of Limitations, the same was not valid as petitioner did not receive the accepted copy thereof. And even assuming that the Waiver dated September 30, 2014 was validly executed, still the assessment for the 1st and 2nd quarters of TY 2011 for VAT and for January to August of TY 2011 for EWT had already prescribed.

The witness further declared that petitioner rejected respondent's assessment for: (1) deficiency IT and VAT on its alleged undeclared income from unaccounted expenses; (2) deficiency IT on the excess tax credit carried forward to the succeeding period and excess Minimum Corporate Income Tax (MCIT) carried forward to the succeeding period; (3) deficiency VAT on the disallowed input tax; (4) deficiency VAT on the input tax carried forward to the succeeding quarter; and (5) deficiency DST.

On December 1, 2017, petitioner formally offered its documentary evidence[19], which were all admitted in the Resolution[20] dated January 10, 2018.

To prove his defense, respondent presented his lone witness, **RO Marilyn D. Guerzon** who testified[21] that she holds the position of Revenue Officer I assigned at Revenue District Office No. 48 in West Makati. She learned about the

[19] Docket, pp. 394-405.
[20] Docket, pp. 645-646.
[21] Exhibit R-11, Judicial Affidavit, pp. 327-333.

case when she received a Memorandum of Assignment dated May 19, 2014 issued by Regional Director Nestor S. Valeroso, directing her to continue the audit and investigation of petitioner's internal revenue taxes for TY 2011, pursuant to electronic Letter of Authority (*e*LOA) which he issued on November 16, 2012. Petitioner was informed of such re-assignment via a Letter dated May 30, 2014, received on June 9, 2014 through its authorized representative, Marlene Ramos.

Based on the BIR record, after receipt of the LOA by petitioner, RO Roberto C. Taylo issued a First Notice dated January 9, 2013 for petitioner's presentation of its books of accounts and accounting records pertinent to the investigation of its internal revenue tax for TY 2011. This was followed by a Second and Final Notice issued on March 11, 2013, requiring petitioner to submit additional documents for audit. After conducting the tax investigation, she prepared a Memorandum recommending issuance of Assessment Notice against petitioner.

The PAN with attached Details of Discrepancies was issued on December 19, 2014 and received by petitioner on even date. The Formal Assessment Notice (FAN) with attached Assessment Notices and Details of Discrepancies, all dated January 13, 2015, followed which petitioner received on January 14, 2015.

Subsequently, an FDDA dated August 18, 2016 with attached Details of Discrepancies was issued to petitioner. The Details of Discrepancies contained the factual and legal bases of the assessment and how the amounts indicated therein were arrived.

On August 6, 2018, respondent was deemed to have rested his case upon admission of all his documentary exhibits.[22]

On November 14, 2018, the instant case was submitted for decision considering petitioner's Memorandum[23] filed on

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[22] Docket, pp. 657-658.
[23] Docket, pp. 674-710.

October 22, 2018, *sans* respondent's Memorandum, despite directive.[24]

THE ISSUES

The parties submitted the following issues[25] for the resolution of the Court, *viz.*:

1. Whether the revenue officer was authorized to conduct the examination;

2. Whether the assessment has prescribed;

3. Whether the subject waiver was valid;

4. Whether the subject assessment lacks factual and legal basis; and,

5. Whether the petitioner is liable for the alleged IT, VAT, WTC and EWT for TY 2011 in the aggregate amount of Twenty Million Five Hundred Forty Thousand Five Hundred Five and 43/100 Pesos (₱20,540,505.43).

THE COURT'S RULING

As in other assessment cases, the timeliness of the filing of the instant Petition for Review must first be determined.

Section 228[26] of the National Internal Revenue Code (NIRC) of 1997, as amended, provides that a taxpayer

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[24] Resolution, docket, p.714.

[25] Issue, JSFI, docket, p. 337.

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

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

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

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 adversely affected by the decision of the CIR may appeal to the Court of Tax Appeals (CTA) within thirty (30) days from receipt of the adverse decision; otherwise, the same shall become final, executory and demandable.

It is undisputed that petitioner received the assailed FDDA with attached Details of Discrepancies on August 24, 2016. In the FDDA, respondent denied petitioner's protest and reiterated the deficiency assessment for IT, VAT, EWT and DST, including penalties and interests, for TY 2011 in the total amount of ₱20,540,505.43. Thus, petitioner had thirty (30) days from August 24, 2016, or until September 23, 2016, within which to appeal the FDDA before this Court. Evidently, the instant Petition for Review was seasonably instituted on September 23, 2016, vesting this Court with the authority to take cognizance of the same pursuant to Section 7(a)(1) of Republic Act (RA) No. 1125, as amended by RA No. 9282.[27]

On the merit of the Petition, petitioner claims that respondent's assessment is invalid for lack of authority on the part of the revenue officer who conducted the tax investigation, hence must be cancelled and withdrawn. Allegedly, in the LOA-051-2012-00000381 dated November 16, 2012, only RO Roberto Taylo and Group Supervisor Arnaldo Rase were authorized to examine its books of accounts and other accounting records for all internal revenue taxes for TY 2011. However, it was RO Marilyn D. Guerzon, whose name did not appear in the LOA, who actually conducted the tax audit pursuant to a mere MOA in clear violation of Section 13 of the NIRC of 1997, as amended.

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sixty (60) days from filing of the protest, all relevant supporting documents shall have been submitted; otherwise, the assessment shall become final.

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 (30) days from receipt of the said decision**, or from the lapse of the one hundred eighty (180)-day period; otherwise, the decision shall become final, executory and demandable. (*Emphasis supplied*)

[27] Sec. 7. *Jurisdiction*. - The CTA shall exercise:
(a) Exclusive appellate jurisdiction to review by appeal, as herein provided:
(1) Decisions of the Commissioner of Internal Revenue in cases involving disputed assessments, refunds of internal revenue taxes, fees or other charges, penalties in relation thereto, or other matters arising under the National Internal Revenue Code or other laws administered by the Bureau of Internal Revenue; xxx.

An audit process normally commences with the issuance of a Letter of Authority or LOA by the CIR. The LOA gives notice to the taxpayer that it is under investigation for possible deficiency tax assessment and at the same time, authorizes or empowers the RO named therein to examine, verify, and scrutinize a taxpayer's books of accounts and records in relation to internal revenue tax liabilities for a particular period.

In other words, before a particular taxpayer may be validly examined for possible tax liability, a LOA must first be issued to the concerned RO authorizing him/her to conduct the tax examination. Without such LOA, the resulting assessment or examination is a complete nullity.

Section 13 of the same tax code defines LOA as the authority given to the appropriate RO assigned to perform assessment functions. It empowers the said RO to examine the books of accounts and other accounting records of a taxpayer within his jurisdiction for the purpose of collecting the correct amount of tax. It reads:

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

Clearly, there must be a grant of authority before any RO may conduct an examination or assessment. This is because the absence of authority of the concerned revenue officer to conduct the audit goes into the validity of the assessment that will subsequently be issued. Without such authority, the assessment or examination is a nullity.[28]

The elucidation of the Supreme Court in the case of *Medicard Philippines, Inc. vs. Commissioner of Internal Revenue*[29] on the matter is instructive, thus:

> ***The absence of an LOA violated MEDICARD's right to due process***
>
> An LOA is the authority given to the appropriate revenue officer assigned to perform assessment functions. It empowers or enables said revenue officer to examine the books of account and other accounting records of a taxpayer for the purpose of collecting the correct amount of tax. An LOA is premised on the fact that the examination of a taxpayer who has already filed his tax returns is a power that statutorily belongs only to the CIR himself or his duly authorized representatives. Section 6 of the NIRC clearly provides as follows:
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>> **SEC. 6.** *Power of the Commissioner to Make Assessments and Prescribe Additional Requirements for Tax Administration and Enforcement.* -
>>
>> (A) **Examination of Return and Determination of Tax Due.**- After a return has been filed as required under the provisions of this Code, **<u>the Commissioner or his duly authorized representative</u> 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

[28] *Commissioner of Internal Revenue vs. Sony Philippines, Inc.*, G.R. No. 178697, November 17, 2010.
[29] G.R. No. 222743, April 5, 2017.

> taxpayer. xxx (*Emphasis and underlining ours*)

Based on the afore-quoted provision, it is clear that unless authorized by the CIR himself or by his duly authorized representative, through an LOA, an examination of the taxpayer cannot ordinarily be undertaken. The circumstances contemplated under Section 6 where the taxpayer may be assessed through best-evidence obtainable, inventory-taking, or surveillance among others has nothing to do with the LOA. These are simply methods of examining the taxpayer in order to arrive at the correct amount of taxes. Hence, unless undertaken by the CIR himself or his duly authorized representatives, other tax agents may not validly conduct any of these kinds of examinations without prior authority.

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In the case of *Commissioner of Internal Revenue v. Sony Philippines, Inc.*, the Court said that:

> Clearly, there must be a grant of authority before any revenue officer can conduct an examination or assessment. Equally important is that the revenue officer so authorized must not go beyond the authority given. **<u>In the absence of such an authority, the assessment or examination is a nullity</u>**. (*Emphasis and underlining ours*)

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Contrary to the ruling of the CTA *en banc*, an LOA cannot be dispensed with just because none of the financial books or records being physically kept by MEDICARD was examined. To begin with, Section 6 of the NIRC requires an authority from the CIR or from his duly authorized representatives before an examination 'of a taxpayer' may be made. The requirement of authorization is therefore not dependent on whether the taxpayer may be required to physically open his books and financial records but only on whether a taxpayer is being subject to examination.

x x x

That the BIR officials herein were not shown to have acted unreasonably is beside the point because the issue of their lack of authority was only brought up during the trial of the case. What is crucial is whether the proceedings that led to the issuance of VAT deficiency assessment against MEDICARD had the prior approval and authorization from the CIR or her duly authorized representatives. Not having authority to examine MEDICARD in the first place, the assessment issued by the CIR is inescapably void."

In relation to the foregoing, Section C(1) and (5) of Revenue Memorandum Order (RMO) No. 43-90 or *"Amendment of Revenue Memorandum Order No. 37-90 prescribing revised policy guidelines for Examination of Returns and Issuance of Letters of Authority to Audit"*, highlights the importance of LOA and explicitly requires the issuance of a new LOA in cases of re-assignment/transfer of cases to another ROs for tax examination or audit, viz.:

C. Other policies for issuance of L/As.

1. **All audits/investigations, whether field audit or office audit, should be conducted under a Letter of Authority**.

xxx xxx xxx

5. **Any re-assignment/transfer of cases to another RO(s), and revalidation of L/As which have already expired, shall require the issuance of a new L/A, with the**

> **corresponding notation thereto, including the previous L/A number and date of issue of said L/As.**" xxx (*Emphases supplied*)

In the present case, the examination of petitioner's internal revenue taxes for TY 2011 commenced when LOA-051-2012-00000381 dated November 16, 2012 was issued by Regional Director Nestor S. Valeroso authorizing RO Roberto Taylo and Group Supervisor Arnaldo Rase to examine the books of account and other accounting records of petitioner for all internal revenue taxes for TY 2011. The record however is bereft of any indication that the two authorized ROs conducted the audit as directed, although it appears that RO Roberto Taylo sent two (2) notices requesting petitioner to submit documents in relation to the audit. Subsequently, the same Regional Director issued MOA dated May 19, 2014, directing RO Marilyn D. Guerzon to continue the tax examination process. After the examination conducted[30], RO Guerzon found petitioner liable for internal revenue taxes and recommended in her Memorandum sent to BIR Revenue Region No. 8-Makati City, the issuance of corresponding assessment notices against petitioner. On December 19, 2014, the recommended PAN with attached Details of Discrepancies was issued assessing petitioner for deficiency IT, VAT, EWT, and DST for TY 2011 in the total amount of ₱16,864,603.94. It was followed by the FAN dated January 13, 2015 and finally, by the assailed FDDA dated August 18, 2016 denying petitioner's protest against the FAN and increasing the amount of tax liability to ₱20,540,505.43.

Evidently, no LOA was issued naming and authorizing RO Marilyn D. Guerzon to conduct the tax audit against petitioner. Her action was merely based on the MOA dated May 19, 2014 directing her to continue the tax audit. Hence, the deficiency tax assessments issued against petitioner, based on her finding and recommendation after audit, is void *ab initio*.

To repeat, before any revenue officer can conduct a tax audit or examination, there must be a valid grant of authority for that purpose from the CIR. Section 6 (A) of

[30] Exhibits "R-11" and "R-11-a".

the NIRC of 1997, as amended, vests the CIR the power to authorize the examination of any taxpayer and the assessment of the correct amount of tax due, to wit:

> **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.

While "taxes are the lifeblood of the government", the power to tax has its limits, in spite of all its plenitude.[31] Even as we concede the inevitability and indispensability of taxation, it is a requirement in all democratic regimes that it be exercised reasonably and in accordance with the prescribed procedure. [32]

In view of the foregoing, this Court finds it unnecessary to belabor on the remaining issues raised by the parties, for it is well-settled that a void assessment bears no valid fruit.[33]

WHEREFORE, the Petition for Review is **GRANTED**. Accordingly, the Final Decision on Disputed Assessment dated August 18, 2016, assessing petitioner for deficiency Income Tax, Value-added Tax, Expanded Withholding Tax and Documentary Stamp Tax, including interests and penalties, in the aggregate amount of ₱20,540,505.43 for

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[31] *Commissioner of Internal Revenue vs. Metro Star Superama, Inc.*, G.R. No. 185371, December 8, 2010.

[32] *Commissioner of Internal Revenue vs. United Salvage and Towage (Phils.), Inc.*, G.R. No. 197515, July 2, 2014.

[33] *Commissioner of Internal Revenue vs. Liquigaz Philippines Corporation,* G.R. Nos. 215534 and 215557, April 18, 2016.

the taxable year 2011, is hereby **CANCELLED and SET ASIDE**.

SO ORDERED.

ESPERANZA R. FABON-VICTORINO
Associate Justice

We concur:

ON LEAVE
ROMAN G. DEL ROSARIO
Presiding Justice

CATHERINE T. MANAHAN
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.

ESPERANZA R. FABON-VICTORINO
Associate Justice
Acting Chairperson

CERTIFICATION

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

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Acting Presiding Justice