REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

SECOND DIVISION

JED MARKETING, CORP. Petitioner,	**CTA CASE NOS. 9687**
-versus-	Members: **Castañeda, Jr.,** *Chairperson,* **Mindaro-Grulla,** and, **Bacorro-Villena,** *JJ.*
COMMISSIONER OF INTERNAL REVENUE, Respondent.	Promulgated: JUN 10 2020 3:45 p.m.

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DECISION

CASTAÑEDA, JR., *J.*:

THE CASE

This *Petition for Review* filed by petitioner JED Marketing, Corp. on September 13, 2017, prays for the cancellation and withdrawal of the *Final Decision* dated August 9, 2017 issued by respondent Commissioner of Internal Revenue for its alleged deficiency income tax for taxable year ending 2007 in the amount of ₱22,640,164.05, inclusive of interest.[1]

THE PARTIES

Petitioner JED Marketing, Corp. is a corporation duly organized and existing under Philippine laws, with business address at Lot 91-A Bagsakan Road, FTI Complex, Taguig City.[2] It is registered with the Bureau of Internal Revenue (BIR) with Taxpayer Identification Number (TIN) No. 000-777-176-000.[3]

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[1] Summary of the Case, Pre-Trial Order dated February 21, 2018, Docket – Vol. I, p. 266.
[2] Exhibits "P-1", "P-1-A", and "P-1-B", Docket – Vol. I, pp. 284 to 293.
[3] Exhibit "P-2", Docket – Vol. I, pp. 294 to 295.

Respondent, on the other hand, is the duly appointed Commissioner of Internal Revenue, vested under the appropriate laws with the authority to carry out the functions, duties and responsibilities of said office, including, *inter alia*, the power to decide disputed assessments, grant tax refunds and issue tax credit certificates, pursuant to the provisions of the National Internal Revenue Code (NIRC), as amended, and other laws, rules and regulations. He may be served with summons, notices and other processes at the Legal Division, Bureau of Internal Revenue (BIR), Revenue Region No. 8, 2nd Floor, BIR Bldg., 313 Sen. Gil Puyat Avenue, Makati City.[4]

ANTECEDENTS (ADMINISTRATIVE LEVEL)

On January 26, 2011, petitioner received the BIR's *Formal Assessment Notice* (FAN) dated January 24, 2011, with attached *Details of Discrepancies*,[5] finding petitioner liable for deficiency income tax in the amount of ₱18,924,990.20, inclusive of interest, for taxable year 2007. The BIR likewise assessed petitioner the amount of ₱25,000.00 as compromise penalty.

Petitioner then filed with the BIR its protest letter dated February 2, 2011,[6] protesting the said FAN.

Subsequently, Regional Director Nestor S. Valeroso issued a *Final Decision on Disputed Assessment* (FDDA) dated August 10, 2012, with attached *Details of Discrepancies*,[7] denying petitioner's protest, and informing petitioner that it is liable for deficiency income in the total amount of ₱22,640,164.15, inclusive of interest and surcharge, for taxable year 2007. The said document was received by petitioner on August 29, 2012.

Consequently, on September 14, 2012, petitioner filed with the BIR its *Legal Petition Notice – Protest for Review* dated September

[4] Par. 1, Facts Admitted, *Joint Stipulation of Facts and Issues* (JSFI), Docket – Vol. I, p. 258.
[5] Exhibit "P-3", Docket – Vol. I, pp. 296 to 298; Par. 2, Facts Admitted, JSFI, Docket – Vol. I, p. 258.
[6] Exhibit "P-4", Docket – Vol. I, pp. 299 to 306.
[7] Exhibit "P-5", Docket – Vol. I, pp. 318 to 319; Par. 3, Facts Admitted, JSFI, Docket – Vol. I, p. 259.

12, 2012,[8] appealing to respondent the said FDDA dated August 10, 2012.

Thereafter, respondent issued the *Final Decision* dated August 9, 2017,[9] affirming the demand for payment in the aggregate amount of ₱22,640,164.15, as embodied in the FDDA dated August 10, 2012.

PROCEEDINGS BEFORE THIS COURT

On September 13, 2017, petitioner filed the instant *Petition for Review*.[10]

Respondent filed his *Answer*, *via* registered mail, on November 24, 2017,[11] interposing the following special and affirmative defenses, to wit:

> "**SPECIAL AND AFFIRMATIVE DEFENSES**
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> 7) Respondent reiterates and repleads the preceding paragraphs of the Answer as part of the Special and Affirmative Defenses.
>
> 8) The petitioner alleged that the assessment against it is void for violating due process, however, in its Petition for Review, the petitioner failed to provide the specific factual basis of the alleged violation of due process.
>
> 9) Petitioner alleged that it was not accorded due process, however, said allegation is contrary to the facts and legal findings of the Commissioner of Internal Revenue. The Commissioner of Internal Revenue on its decision dated August 9, 2017 found that:
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> > '**Records show that all these requirements have been complied with in the assessment of JED's tax deficiency**. The NIC (Notice of Informal Conference), PAN (Preliminary Assessment Notice), FAN (Formal Assessment Notice), and FDDA (Final Decision on Disputed Assessment) have been all complied with. The periods provided for JED to present its side have given, in some cases, even

[8] Exhibit "P-6", Docket – Vol. I, pp. 320 to 327.
[9] Exhibit "P-7", Docket – Vol. I, pp. 352 to 375; Par. 4, Facts Admitted, JSFI, Docket – Vol. I, p. 259.
[10] Docket – Vol. I, pp. 10 to 23.
[11] Docket – Vol. I, pp. 153 to 181.

longer than the law required. It cannot be denied that JED was given all the opportunities to present its side verbally and in writing. From the start of the investigation up to its administrative appeal, JED has sent at least thirty-five (35) letters with varying nature and tenor. These letters have reached not only the BIR, but the Office of the President, Ombudsman, Civil Service Commission, and Commission on Audit. JED letter were not confined to raising arguments against the assessment alone, but to accusing the involved revenue officials of not performing their duties and extended into requesting the Ombudsman to conduct an investigation on them, which was duly denied in the Order of the Ombudsman dated June 17, 2012. On their part, the revenue officials of RDO No. 44 tried to answer the letters of JED, in fact they have sent at least (20) letters ranging from notices, follow-ups and replies. **As JED's letters were peppered with various provisions from different laws, the letters and the entire docket had to be repeatedly indorsed to the RR8 Legal Division for their opinion concerning the legal arguments. This resulted to further delaying the assessment and showing confusion on the status and location of the docket as the RR8 and RDO No. 44 were not co-located**.

Neither can it be claimed that JED was not fully informed in writing of the law and facts on which its assessment is based. At the onset of the examination, JED was provided with LOA and the list of documents that will be examined by the assigned RO. Despite this, and two subsequent notices [,] JED only submitted vouchers, receipts, invoices, and its books of accounts, which did not have any contents. Nevertheless, examination ensued and after the examination, JED was informed of the RO's findings together with RO's worksheet, which contained a schedule of the vouchers along with their particulars, and was provided as NIC. After which, they were given more than enough time, even more than fifteen days mandated by law, to submit any response or opposition to the findings of the RO, which it failed to do. Still, its argument against the findings during the informal conference, was taken into consideration and the deficiency Value-Added Tax assessment was removed when the PAN was issued. The law does not require an updated NIC for holding another informal conference because taxpayer is expected to thresh out all its opposition to RO's computations during the informal conference. More importantly, the taxpayer still has the chance to reply to the PAN and protest to the FAN. It is worthy that the computation of the deficiency income tax assessment did not change starting from the informal conference up to the PAN, FAN, and the FDDA. Thus, JED's repeated claim that it did not receive the details of how the computation was arrived at is belied by the records showing that the worksheet used for the computation was received by its employee, along with the NIC. The details were again provided during the mediation conference had at the Ombudsman on JED's request. While it is true that the PAN, FAN, and FDDA did not include a copy of this worksheet, it does not mean that there [was] lack of due process. The assessment [was] issued following the format prescribed by RR No. 12-99, which does not require the RO's working papers to be included.

Considering these, there is no doubt that JED was accorded due process during the assessment. X X X" (Emphasis Supplied.)

10) Petitioner was duly apprised of the factual and legal basis of the assessment. If the taxpayer is able to intelligently argue its case and elucidate the reasons for the assessment, then it cannot contradict itself by asserting that it was not informed of the law and facts on which the assessment was made. In the case [of] Sevilla vs Commissioner of Internal Revenue, CTA Case No. 6211, October 4, 2004, this Honorable Court ruled that:

'The respondent though may not have provided the specific provisions of the National Internal Revenue Code or other internal revenue laws as bases for the assessments but by indicating the kind of tax petitioners were liable was a substantial compliance with the requirements of Section 228 of the National Internal Revenue Code of 1997 (NIRC). In a fair play point of view the petitioners were after all, not left in confusion and grasping in the dark for explanations of the assessment. This is easily discernible from petitioner's protest letter (BIR Records, page 180) dated May 31, 2000. This court in the case of Subic Power Corporation v. Commissioner of Internal Revenue (CTA Case No. 6059, May 8, 2003) held that:

'While we concede that the mere filing of a protest letter does not automatically mean that the requirements of Section 228 has not been violated, **if the taxpayer is able to intelligently argue its case and elucidate the reasons for the**

> **assessment**, as in this case, then it cannot contradict itself by asserting that it was not informed of the law and facts on which the assessment was made.
>
> x x x
>
> Further, it is our considered opinion that the phrase 'in writing' under Section 228 does not exclusively mean written words. 'Writings' consist of letters, words, or numbers, or their equivalent, set down by handwriting, typewriting, printing, Photostatting, photographing, magnetic impulse, mechanical or electronic recording, or other form of data compilation (Blacks Law Dictionary), Sixth Edition, page 1609). Indubitably, figures are also 'writings' and if the numerical presentation is understandable enough, then there is no reason why we should automatically reject the same as adequate compliance with the law. **It must be stressed that the underlying reason for the law is the basic constitutional requirement that 'no person shall be deprived of his property without due process of law'. Parenthetically, in whatever form and manner, as long as the taxpayer is informed of how the assessment was arrived at, then Section 228 has not been violated.** And if petitioner had already been informed during the preliminary stage of the bases for the assessment, then it could not insist that it was not informed of the law and the facts on which the assessment was based (Subic Power Corporation vs. Commissioner of Internal Revenue, supra). Indeed, the due process requirement in the instant petition been satisfactorily met.' (Emphasis Provided)

11) It must be considered that the petitioner aside from the legal protest dated February 2, 2011, made at least other 11 legal protests, notices, transmittals, and manifestations, to wit:

Date	Details:
February 10, 2011	Legal Final Protest Notice-Reconsideration

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February 21, 2011	Legal Petition Notice for Speediest Resolution of a Formal Protest
March 14, 2011	Legal Final Notice Prior Mediation Conference
April 4, 2011	Legal Petition Notice
April 29, 2011	Legal Follow-Up Notice (First Notice)
December 27, 2011	Legal Petition Notice
February 2, 2012	Legal Follow-up Notice – (1st Notice)
February 28, 2012	Legal Evidence Transmittal Notice
May 4, 2012	Legal Protest Notice – a reconsideration and not a reinvestigation
May 4 and 7, 2017	Legal Manifestation and Petition Notice
June 13, 2012	Legal Manifestation and Petition Notice

12) ***Disallowance of petitioner's expenses or cost amounting to Php 34,347,478.61 is consequence of petitioner's failure to substantiate its business expenses, in other words, petitioner failed to submit relevant documents to support its business expenses.*** Under the Tax Code, no deduction shall be allowed 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.

13) Petitioner['s] allegation that its voucher is an evidence against tax assessment is contrary to the facts and legal finding of the Commissioner of Internal Revenue. The Commissioner of Internal Revenue in its decision dated August 9, 2017 found that:

> 'In ruling that the vouchers submitted by JED were irrelevant supporting document to disprove tax assessment, BIR RDO Rosario stated that:
>
> 'xxx A voucher is an accounting document representing...an internal intent to make payment to an external entity, such as vendor or service provider. Intent to make payment fall short of Section 34 (A) of the Tax Code which requires that ordinary and necessary expenses must be paid or incurred during the taxable year. Stated otherwise, the law requires that before expenses or costs may be allowed as deduction from the gross income, it must be shown to have been actually paid and not merely an intent to make payment.
>
> Further, the FDDA cited in the case of Towne & City Development Corporation vs. Court of Appeals, where the Supreme Court held that:
>
> > 'It should be noted that a voucher is not necessarily an evidence of payment. It

> is merely a way or method of recording or keeping track of payment made. A procedure adopted by companies for the orderly and proper accounting of fund disbursed. Unless it is supported by an actual payment like the **issuance of a check which is subsequently encashed or negotiated, or an actual payment of cash duly receipted** for as is customary among businessmen, a voucher remains a piece of paper having no evidentiary weight'. (Emphasis supplied)

14) In line with the decision of the Supreme Court in the case of H. Tambunting Pawnshop, Inc. vs. Commissioner of Internal Revenue, the petitioner should have presented proper document required by law to substantiate its expenses.

15) Petitioner should have presented the official receipts or invoices to prove its claim as provided for under Section 237 of the National Internal Revenue Code of 1997, to wit:

> '**SEC. 237. Issuance of Receipts or Sales or Commercial Invoices.-** All persons subject to an internal revenue tax shall, for each sale and transfer of merchandise or for services rendered valued at Twenty-Five pesos (P25.00) or more, issued duly registered receipts or sale or commercial invoices, prepared at least induplicate, showing the date of transaction, quantity, unit cost and description of merchandise or nature of service; Provided, however, That where the receipt is issued to cover payment made as rentals, commissions, compensation or fees, receipts or invoices shall be issued which shall show the name, business style, if any, and address of the purchase, customer or client.
>
> The original of each receipt or invoice shall be issued to the purchaser, customer or client at the time the transaction is effected, who, if engaged in business or in the exercise of profession, shall keep and preserve the same in his place of business for a period of three (3) years from the close of the taxable year in which such invoice or receipt was issued, while the duplicate shall be kept and preserved by the issuer, also in his place of business, for a like period.
>
> The Commissioner may, in meritorious cases, exempt any person subject to internal revenue tax from compliance with the provisions of this Section.'

16) In the aforementioned Supreme Court Case H. Tambunting Pawnshop, Inc. vs. Commissioner of Internal Revenue, the Supreme Court ruled:

> 'With regard to the misclassified items of expenses, petitioner's statements were self-serving, likewise it failed to substantiate its allegations by clear and convincing evidence as provided under the foregoing provision of law.
>
> Bearing in mind the principle in taxation that deductions from gross income partakes the nature of tax exemptions which are construed in strictissimi juris against the taxpayer, the Court en banc is not inclined to believe the self-serving statements of petitioner regarding the misclassified items of office, supplies, advertising and rent expenses.
>
> Among the expenses allegedly incurred, courts may consider only those supported by credible evince and which appear to have been genuinely incurred in connection with the trade or business of the taxpayer.
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> x x x x
>
> As previously discussed, the proper substantiation requirement for an expense to be allowed is the official receipt or invoice. While the rental payments were subjected to the applicable expanded withholding taxes, such returns are not the documents required by law to substantiate the rental expense. Petitioner should have submitted official receipts to support its claim.
>
> Moreover, the issue on the submission of cash vouchers as evidence to prove expenses incurred has been addressed by this Court in the assailed Resolution, to wit:
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>> 'The trend then was to allow deductions based on cash vouchers which are signed by the payees. It bears to note that the cases cited by petitioner are pronouncements by this Court in 1980, 1982 and 1989.
>>
>> However, latest jurisprudence has deviated from such interpretation of the law. Thus, this Court held in the case of Pilmico-Mauri Foods Corporation vs. Commissioner of Internal Revenue C.T.A. Case No. 6151, December 15, 2004;

> [P]etitioner's contention that the NIRC of 1977 did not impose substantiation requirements on deductions from gross income is bereft of merit. Section 238 of the 1977 Tax Code [now Section 237] provides:
>
> x x x
>
> From the foregoing provision of law, a person who is subject to an internal revenue tax shall issue receipts, sales or commercial invoices, prepared at least in duplicate. The provision likewise imposed a responsibility upon the purchaser to keep and preserve the original copy of the invoice or receipt for a period of three years from the close of the taxable year in which the invoice or receipt was issued. The rationale behind the latter requirement is the duty of the taxpayer to keep adequate records of each and every transaction entered into in the conduct of its business. So that when their books of accounts are subjected to a tax audit examination, all entries therein could be shown as adequately supported and proven as legitimate business transactions. Hence, petitioner's claim that the NIRC of 1977 did not require substantiation requirement is erroneous.

In order that cash vouchers may be given probative value, these must be validated with official receipts.' (Emphasis supplied)

17) In its Petition for Review, petitioner cited BIR Ruling No. DA-(TAR-001) 009, dated January 13, 2009 and other BIR Rulings, however, it must be noted that BIR Rulings obtained by other entities that may or may not be similarly situated as petitioner. BIR Rulings contain the following or similar caveat:

> 'This ruling is being issued on the basis of the foregoing facts as represented. However, if upon investigation, it will be disclosed that the facts are different, then this ruling shall be considered as null and void.'

18) Moreover, there is no evidence on record that petitioner requested for and relied on a BIR ruling confirming its exemption from Sec. 237 of the Tax Code.

19) The petitioner is barred from raising the issue of prescription of period to collect considering that the petitioner questions and put into issue the validity of the assessment in this case. It must be noted that administrative collection presupposes that there is already a final and executory assessment, and as far as the petitioner is concerned, they are considering the assessment as void and not final and executory.

20) Moreover, petitioner have resorted to delaying tactics, as found by the BIR's Commissioner Office, factual backgrounds show that 'from the start of the investigation up to its administrative appeal, JED has sent at least thirty-five (35) letters with varying nature and tenor. These letters have reached not only the BIR, but the Office of the President, Ombudsman, Civil Service Commission, and Commission on Audit. JED's letter were not confined to raising arguments against the assessment alone, but to accusing the involve revenue officials of not performing their duties and extended into requesting the Ombudsman to conduct an investigation on them, which was duly denied in the Order of the Ombudsman dated June 17, 2012. On their part, the revenue officials of RDO No. 44 tried to answer the letters of JED. In fact, they have sent at least (20) letters ranging from notices, follow-ups, and replies. As JED's letters were prepared with various provisions form [*sic*] different laws, the letters and the entire docket had to be repeatedly indorsed to the RR 8 Legal Division for their opinion concerning the legal arguments. This resulted to further delaying the assessment and showing confusion on the status and location of the docket as the RR8 and RDO No. 44 were not co-located.'

21) The running of the 5 years statute of limitations as provided under 1997 NIRC is not applicable in this case but rather the 10[-]year prescriptive period pursuant to Section 222(a) of the NIRC which states that:

> 'SEC. 222. Exceptions as to the Period of Limitation of Assessment and **Collection of Taxes.**
>
> (a) In the case of a **false or fraudulent return** with intent to evade tax or of failure to file a return, the tax may be assessed, or **a proceeding in court for the collection of such tax may be filed without assessment, at any time within ten (10) years after the discovery of the falsity, fraud or omission**: Provided, That in a fraud assessment which has become final and executory, the fact of fraud shall be judicially taken cognizance of in the civil or criminal action for the collection thereof.' (Emphasis Provided)

22) In this case, the petitioner has substantial undeclared income and overstated deduction. The petitioner declared Php 889,453.00 taxable income per ITR, while the petitioner is being assessed for basic deficiency income tax amounting to Php12,021,617.51. Petitioner declared cost per ITR is Php 88,055,877.00, however, its overclaimed cost amounts to 34,347,478.61. The 1997 Tax Code provides that under declaration of sales, receipts or income in an amount exceeding 30 percent of that declared per return, and overstatement of the deductions claimed by an amount exceeding 30 percent shall be construed as substantial, thus, creating a prima facie case of a false or fraudulent return. Thus, the petitioner's 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.

23) The allegation of the petitioner that the period to collect tax deficiency taxes pursuant to Section 222 (c) of the 1997 Tax Code has already prescribed does not have a leg to stand on. The Tax Code of 1997, as amended, provides instances when the running of the statute of limitations on the assessment and collection of national internal revenue taxes could be suspended, even in the absence of a waiver, under Section 223 thereof which reads:

> '**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 reinvestigation 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: X X X.' (Emphasis supplied.)

38) In the case of Commissioner of Internal Revenue vs. Philippines Global Communication, Inc. the Supreme Court held that:

> 'Revenue Regulations No. 12-85, the Procedure Governing Administrative Protests of Assessment of the Bureau of Internal Revenue, issued on 27 November 1985, defines the two types of protest, the request for reconsideration and the request for reinvestigation, and distinguishes one from the other in this manner:

> Section 6. Protest. — The taxpayer may protest administratively an assessment by filing a written request for reconsideration or reinvestigation specifying the following particulars:
>
> x x x x
>
> For the purpose of protest herein —
>
> (a) *Request for reconsideration* — refers to a plea for a re-evaluation of an assessment on the basis of existing records without need of additional evidence. It may involve both a question of fact or of law or both.
>
> (b) ***Request for reinvestigation* refers to a plea for re-evaluation of an assessment on the basis of newly-discovered evidence or additional evidence that a taxpayer intends to present in the investigation**. It may also involve a question of fact or law or both. (Emphasis supplied.)

The main difference between these two types of protests lies in the records or evidence to be examined by internal revenue officers, whether these are existing records or newly discovered or additional evidence. A re-evaluation of existing records which results from a request for reconsideration does not toll the running of the prescription period for the collection of an assessed tax. Section 271 distinctly limits the suspension of the running of the statute of limitations to instances when reinvestigation is requested by a taxpayer and is granted by the CIR.'

39) As disclosed by the facts of this instant case, it must be noted that in this case, the petitioner requested twice for reinvestigation when it filed the following:

a) 'Legal Petitioner Notice' dated April 4, 2011, and 'Legal Transmittal Notice' for the submission of new evidence consisting of one box containing 432 original JED vouchers filed on April 6, 2011.

   Attached hereto and forming integral part hereof are Annexes 'A' and 'B', photocopies of 'Legal Petitioner Notice' dated April 4, 2011, and 'Legal Transmittal Notice' dated April 6, 2011, respectively.

b) Petitioner's Petition for Review dated September 12, 2014 with attached cancelled checks filed with Commissioner of Internal Revenue on September 14, 2012.

40) The petitioner requested twice for reinvestigation and the same was considered by the respondent. It is the rule that averments in the pleadings, not the title, are controlling in determining the nature of the proceeding.

41) The first request for reinvestigation can be inferred from the following facts and events:

a) After filing 'Legal Final Protest Notice- A Reconsideration dated February 2, 2011 on February 10, 2011 against the FAN dated January 24, 2011, on April 6, 2011, JED filed a 'Legal Petitioner Notice' dated April 4, 2011, and 'Legal Transmittal Notice' dated April 6, 2011 for the submission of new evidence consisting of one box containing 432 original JED vouchers. The RDO refused to receive the box of evidence on the ground that the docket has already been forwarded to the R.R. 8 Legal Division for legal opinion.

b) JED filed on May 6, 2011, a 'Legal Follow-up Notice (First Notice)' dated April 29, 2011, recounting the events that transpired on April 6, 2011 and arguing that the RO's refusal to accept the documents constitutes an irregularity in the performance of her duties, ...making the assessment 'interruptible'.

Attached hereto and forming integral part hereof is Annex 'C' is the photocopy of 'Legal Follow-up Notice (First Notice)' dated April 29, 2011.

c) Respondent granted JED's request for reinvestigation based on the FDDA dated August 10, 2012 decision, the said FDDA held the following:

'X X X

> **Reinvestigation of the case included the examination of vouchers you submitted in support of your protest**. However, verification disclosed that the said vouchers failed to disprove the findings per Formal Assessment Notice (FAN) dated January 24, 2011. (Emphasis supplied.)

X X X'

42) By filing on April 6, 2011, a 'Legal Petitioner Notice' dated April 4, 2011, and a 'Legal Transmittal Notice' dated April 6, 2011 for the submission of new evidence consisting of one (1) box containing 432 original JED vouchers, petitioner effectively made a plea for re-evaluation of an assessment on the basis of additional evidence. Thus, petitioner requested for reinvestigation.

43) Petitioner's Petition for Review dated September 12, 2014 filed with the Commissioner of Internal Revenue on September 14, 2012 is in reality another reinvestigation or second request for reinvestigation. The said Petition for Review was decided by the Commissioner of Internal Revenue on August 9, 2017.

44) It must be noted that the Petitioner's 'Legal Petition Notice - PROTEST FOR REVIEW' dated September 12, 2014 filed with the Commissioner of Internal Revenue on September 14, 2014 is a request for reinvestigation because it was a plea for re-evaluation of an assessment on the basis of additional evidence, particularly, the petitioner submitted the original copies of cancelled checks to oppose the FDDA dated August 10, 2012.

45) The intention for the petitioner to plea for reinvestigation is clearly shown by petitioner's 'Legal Petition Notice – PROTEST FOR REVIEW' dated September 12, 2014 filed with the Commissioner of Internal Revenue on September 14, 2014, it provides:

> **'CANCELLED CHECKS**
>
> 146. To comply with the FDDA's dispositive portion as stated above, the alleged unsupported cost shall be supported by cancelled checks or checks issued to my suppliers which were, later on, encashed or negotiated, viz; X X X
>
> 147. **The original copies of cancelled checks are arranged and attached** according to the presentation stated in their respective schedules and forms part of the evidentiary documents.'

46) To bolster the arguments that petitioner plead for reinvestigation, on October 11, 2012 and October 22, 2012, the petitioner filed 'Legal Petition Notice – Supplemental Protest to the FDDA' dated October 4, 2012 and 'Legal Petition Notice - Re-Submission of Evidences' dated October 18, 2012, respectively.

Attached hereto and forming integral part hereof are Annexes 'D' and 'E', photocopies of 'Legal Petition Notice – Supplemental Protest to FDDA' dated October 4, 2012 and 'Legal Petition Notice – Re-Submission of Evidences' dated October 18, 2012, respectively.

47) Petitioner's 'Legal Petition Notice – Supplemental Protest to FDDA' dated October 4, 2012 provides:

> 'VOUCHERS AND CANCELLED CHECKS ARE ALLOWED IN CLAIMING COSTS'

While petitioner's 'Legal Petition Notice - Re – Submission of Evidences dated October 18, 2012 provides:

> 'I am submitting a new set of Certified True Copies of Cancelled Checks to be attached and reconciled on the September 12, 2012 Protest Letter. After all, pursuant to RR 12-99, I still have sixty (60) days from the filing of the said protest, or until November 14, 2012, to submit relevant, admissible and material evidences.'

The foregoing clearly show petitioner's plea for re-evaluation of an assessment on the basis of newly discovered or additional evidence that a taxpayer intends to present in investigation.

48) In the aforementioned case of Commissioner of Internal Revenue vs. Philippine Global Communication, Inc. The Supreme Court held that:

> The Court, in Republic v. Lopez, even gave a detailed accounting of the time the BIR spent for each reinvestigation in order to deduct it from the five-year period set at that time in the statute of limitations:
>
> > It is now a settled ruled in our jurisdiction that the five-year prescriptive period fixed by Section 332(c) of the Internal Revenue Code within which the Government may sue to collect an assessed tax is to be computed from the last revised assessment resulting from a reinvestigation asked for by the taxpayer and (2) that where a taxpayer demands a reinvestigation, the time employed in reinvestigating should be deducted from the total period of limitation.
> >
> > x x x x
> >
> > The first reinvestigation was granted, and a reduced assessment issued on 29 May 1954, from which date the Government had five years for bringing an action to collect.
> >
> > The second reinvestigation was asked on 16 January 1956, and lasted until it was decided on 22 April 1960, or a period of 4 years, 3 months, and 6 days, during which the limitation period was interrupted.

> The Court reiterated the ruling in Republic v. Lopez in the case of Commissioner of Internal Revenue v. Sison, 'that where a taxpayer demands a reinvestigation, the time employed in reinvestigating should be deducted from the total period of limitation.' Finally, in Republic v. Arcache, the Court enumerated the reasons why **the taxpayer is barred from invoking the defense of prescription, one of which was that, 'In the first place, it appears obvious that the delay in the collection of his 1946 tax liability was due to his own repeated requests for reinvestigation and similarly repeated requests for extension of time to pay**.' (Emphasis supplied.)

49) The five-year period to collect is suspended from April 6, 2011, when the petitioner filed its first request for reinvestigation, 'Legal Petitioner Notice' dated April 4, 2011 and a 'Legal Transmittal Notice' for the submission of new evidence consisting of one box containing 432 original JED vouchers, until August 9, 2017, when the Commissioner of Internal Revenue issued its final decision regarding Petitioner's Petition for Review petitioner's second request for reinvestigation. It must be noted that the Petitioner [*sic*] for Review was filed with the Commissioner of Internal Revenue on September 14, 2012, within fifteen (15) days from receipt of the FDDA dated August 10, 2012.

50) The burden of proof is on the taxpayer contesting the validity or correctness of an assessment to prove not only that the Commissioner of Internal Revenue is wrong but also that the taxpayer is right (Tan Guan vs. Court of Tax Appeals, et. al., 19 SCRA 903 [1967] Collector of Internal Revenue vs. Bohol Land Transportation Co., 107 Phil 967 [1960])

51) Assessments are presumed correct and official functions are regularly done. The burden of proving that the assessments are not correct rests on the petitioner. All presumptions are in favor of the correctness of tax assessments. (Interprovincial Autobus vs. Collector of Internal Revenue, 98 Phil. 290).

52) Tax assessments by examiners 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 Bureau of Internal Revenue examiner and approved by his superior officers will not be disturbed. All presumptions are in favor of the correctness of tax assessments."

The Pre-Trial Conference was set and held on February 1, 2018.[12] *Petitioner's Pre-Trial Brief* was filed on January 26, 2018,[13] while *Respondent's Pre-Trial Brief* was filed through private courier on January 29, 2018.[14]

In the meantime, the *BIR Records* for the instant case was submitted on December 6, 2017.[15]

The parties submitted their *Joint Stipulation of Facts and Issues* (JSFI) on February 13, 2018.[16] In the Pre-Trial Order dated February 21, 2018,[17] the said JSFI was approved and adopted by this Court, and the Pre-Trial was deemed terminated.

The trial of the case then proceeded.

During trial, petitioner presented its documentary and testimonial evidence. Petitioner offered the testimony of its sole witness, Ms. Rosalie Tanguanco, [18] Assistant Manager of petitioner.

Petitioner filed its *Formal Offer of Evidence* on May 18, 2018.[19] Respondent filed his *Comment (To Petitioner's Formal Offer of Evidence)* through registered mail on May 21, 2018.[20]

In the Resolution dated July 23, 2018,[21] the Court admitted petitioner's Exhibits, *except* for Exhibit "P-42", for failure to submit the original for comparison.

At the hearing held on July 23, 2018,[22] respondent's counsel manifested that he has no witness to present in this case. Upon his motion, respondent's counsel was given five (5) days from the said

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[12] Notice of the Pre-Trial Conference dated December 11, 2017, Docket – Vol. I, pp. 221 to 222; Minutes of the hearing held on, and Order dated, February 1, 2018, Docket – Vol. I, pp. 246 to 247.
[13] Docket – Vol. I pp. 224 to 229.
[14] Docket – Vol. I pp. 238 to 244.
[15] Docket – Vol. I, p. 220.
[16] Docket – Vol. I, pp. 258 to 264.
[17] Docket – Vol. I, pp. 266 to 272.
[18] Exhibit "P-22", Docket – Vol. I, pp. 376 to 383; Minutes of the hearing held on, and Order dated, May 16, 2018, Docket – Vol. I, pp. 278 to 279.
[19] Docket – Vol. I, pp. 280 to 283.
[20] Docket – Vol. I, pp. 399 to 400.
[21] Docket – Vol. I, pp. 410 to 411.
[22] Minutes of the hearing held on, and Order dated, July 23, 2018, Docket – Vol. I, pp. 412 to 413.

date, or until July 28, 2018, to file his *Formal Offer of Evidence*. Petitioner was granted five (5) days to file its comment thereon.

On July 30, 2018, respondent filed, through registered mail, his *Formal Offer of Evidence with Motion to Correct Sub-markings and Description of Exhibits*.[23] Petitioner filed its *Comment to Respondent's Formal Offer of Evidence* on August 9, 2018.[24]

In the Resolution dated August 22, 2018,[25] the Court admitted respondent's Exhibits, *except* for Exhibits "R-2", "R-3", "R-4", "R-5", "R-6", "R-7", "R-8", "R-9", "R-10", "R-11", "R-12", "R-15", "R-16", "R-17", "R-19", and "R-20", for failure to identify the exhibits; and Exhibit "R-14", for failure to identify the exhibit and for failure to present its original for comparison.

On September 12, 2018, respondent filed, through registered mail, his *Motion for Reconsideration and Manifestation [RE: Resolution promulgated on August 22, 2018]*.[26] Petitioner filed its *Comment* on October 11, 2018.[27] The Court, however, denied the said *Motion for Reconsideration and Manifestation* in its Resolution dated February 15, 2019.[28]

The *Memorandum (For the Petitioner)* was filed on September 17, 2018,[29] while the *Memorandum for Respondent* was filed on March 22, 2019.[30]

This case was considered submitted for decision on April 2, 2019.[31]

THE ISSUES

The following are the issues[32] stipulated by the parties for this Court's resolution, *viz*: *Ju*

[23] Docket – Vol. I, pp. 414 to 421.
[24] Docket – Vol. I, pp. 564 to 565.
[25] Docket – Vol. II, pp. 592 to 594.
[26] Docket – Vol. II, pp. 622 to 642.
[27] Docket – Vol. II, pp. 646 to 52.
[28] Docket – Vol. II, pp. 654 to 661.
[29] Docket – Vol. II, pp. 595 to 621.
[30] Docket – Vol. II, pp. 662 to 681.
[31] Resolution dated April 2, 2019, Docket – Vol. I, p. 682.
[32] Issues, JSFI, Docket – Vol. I, p. 259.

> "1. Whether petitioner substantiated with sufficient evidence its business expenses/cost amount to Php34,347,478.61 in accordance with Sec. 34(A)(1)(b) of the National Internal Revenue Code (NIRC) of 1997, as amended.
>
> 2. Whether the disallowance of petitioner's business expenses/cost amounting to Php34,347,478.61 in the instant petition is valid.
>
> 3. Whether the right of the respondent to collect from petitioner the alleged deficiency income taxes covered by Assessment No. IT-LA28110-07-110263 dated January 24, 2011, had already prescribed.
>
> 4. Whether Petitioner is liable to pay the amount of Php22,640,164.05, inclusive of interest, relative to the Final Decision of the Commissioner dated August 9, 2017, pursuant to assessment no. IT-LA2811-07-11-0263 dated January 24, 2011."

Petitioner's arguments:

Petitioner argues that the purported "Unsupported Cost" amounting to ₱34,347,478.61 was duly substantiated by vouchers and/or check payments; that respondent failed to provide the factual basis of the alleged deficiency tax assessment; that the period to collect alleged deficiency taxes pursuant to Section 222(c) of the Tax Code has already lapsed; that the absence of validly issued Letter of Authority (LOA) to conduct the audit renders the present assessment void; that there was denial of due process; and that the FAN dated January 24, 2011 did not set and fix the tax liability, which is still subject to modification of adjustment, rendering it legally infirm.

Respondent's counter-arguments:

Respondent counter-argues that petitioner failed to provide the specific factual basis of the alleged violation of due process; that petitioner was duly apprised of the factual and legal basis of the assessment; that petitioner should have presented official receipts or vouchers to prove its business expenses; and that respondent's right to collect has not yet prescribed.

THE COURT'S RULING

The instant *Petition for Review* is meritorious.

The subject income tax assessment is void, for lack of an LOA.

Petitioner asserts that the absence of a validly issued LOA to conduct the audit renders the present assessment void.

We agree.

In the BIR, the audit process normally commences with the issuance by respondent or his duly authorized representative of an LOA. The LOA gives notice to the taxpayer that it is under investigation for possible deficiency tax assessment; at the same time, it authorizes or empowers a designated revenue officer to examine, verify, and scrutinize a taxpayer's books and records, in relation to internal revenue tax liabilities for a particular period.[33]

The said power of respondent is derived from Section 6(A) of the NIRC of 1997, which provides as follows:

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

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

[33] *Commissioner of Internal Revenue vs. Lancaster Philippines, Inc.,* G.R. No. 183408, July 12, 2017.

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

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

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

In *Medicard Philippines, Inc. vs. Commissioner of Internal Revenue,*[34] the Supreme Court held:

> "**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:
>
>> 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 may authorize the examination</u>** ge

[34] G.R. No. 222743, April 5, 2017.

> **<u>of any taxpayer</u>** 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.
>
> x x x x (Emphasis and underlining Ours)
>
> Based on the afore-quoted provision, it is clear that **<u>unless authorized by the CIR himself or by his duly authorized representative, through an LOA</u>, 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 <u>without prior authority</u>.**
>
> xxx xxx xxx
>
> In the case of *Commissioner of Internal Revenue v. Sony Philippines, Inc.*,[35] 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)
>
> xxx xxx xxx
>
> 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. **<u>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</u>. 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.**
>
> xxx xxx xxx
>
> 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** jr

[35] 649 Phil. 519 (2010).

> **is crucial is whether the proceedings that led to the issuance of VAT deficiency assessment against MEDICARD <u>had the prior approval and authorization from the CIR or her duly authorized representatives</u>. <u>Not having authority to examine MEDICARD in the first place, the assessment issued by the CIR is inescapably void</u>.**" *(Emphases and underscoring supplied)*

Based on the foregoing jurisprudential pronouncements, it is crucial that the proceedings that led to the issuance of a deficiency tax assessment against a taxpayer had the prior approval and authorization of respondent or his duly authorized representatives, **through an LOA**. As a corollary, an LOA must be issued before an examination, and eventual deficiency tax assessment, of a taxpayer may be made. If the revenue officer who conducted the examination of a taxpayer is not so authorized, through an LOA, in the first place, the assessment is inescapably void.

In the present case, there is no showing that an LOA was issued, authorizing a revenue officer to examine petitioner's books of accounts and other accounting records. Such being the case, the present deficiency income tax assessment is inescapably void.

It must be emphasized that in cases filed before this Court, which are litigated *de novo*, party-litigants must prove <u>every minute aspect</u> of their case.[36] Thus, it was incumbent upon respondent to prove that an LOA was issued in examining petitioner for its income tax liability for taxable year 2007 which led to the assessment of deficiency income tax against the latter.

In any event, We find other grounds which render the subject income tax assessment as void.

There was denial of due process for failure to comply with the requirement of ⁊

[36] *Edison (Bataan) Cogeneration Corporation vs. Commissioner of Internal Revenue, et seq.*, G.R. Nos. 201665 and 201668, August 30, 2017; *Commissioner of Internal Revenue vs. Philippine National Bank*, G.R. No. 180290, September 29, 2014; *Commissioner of Internal Revenue vs. United Salvage and Towage (Phils.), Inc.*, G.R. No. 197515, July 2, 2014; *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.

stating the facts and the law on which the proposed assessment is based.

Petitioner contends that there was denial of due process in this case. It points out that respondent's failure to establish the issuance of a *Preliminary Assessment Notice* (PAN) as prescribed under Section 228 of the NIRC of 1997, as amended, and Revenue Regulations (RR) No. 12-99, is a denial of due process.

On the other hand, respondent argues that the said allegation of petitioner is contrary to the facts and his legal findings.

We rule in favor of petitioner.

Section 228 of the NIRC of 1997 reads:

> "Section 228. *Protesting of Assessment.* – **When the Commissioner or his duly authorized representative finds that proper taxes should be assessed, <u>he shall first notify the taxpayer of his findings</u>:** *Provided, however*, that **a preassessment notice** shall **not** be required in the following cases:
>
> (a) When the finding for any deficiency tax is the result of mathematical error in the computation of the tax as appearing on the face of the return; or
>
> (b) When a discrepancy has been determined between the tax withheld and the amount actually remitted by the withholding agent; or
>
> (c) When a taxpayer who opted to claim a refund or tax credit of excess creditable withholding tax for a taxable period was determined to have carried over and automatically applied the same amount claimed against the estimated tax liabilities for the taxable quarter or quarters of the succeeding taxable year; or
>
> (d) When the excise tax due on excisable articles has not been paid; or
>
> (e) When the article locally purchased or imported by an exempt person, such as, but not limited to, vehicles, capital equipment, machineries and spare parts, has been sold, traded or transferred to non-exempt persons.

> **The taxpayer 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.
>
> xxx xxx xxx." *(Emphases ours)*

Based on the foregoing provision, as a general rule, the concerned taxpayer must first be informed that he or she is liable for deficiency taxes through the sending of a preassessment notice or a PAN. Furthermore, the said taxpayer is required to be informed in writing of the law and the facts on which the assessment is made; otherwise, the assessment shall be void.

Implementing the above-quoted Section 228, Section 3 of RR No. 12-99[37] provides, in part, as follows:

> "SECTION 3. ***Due Process Requirement in the Issuance of a Deficiency Tax Assessment. –***
>
> 3.1 Mode of procedure in the issuance of a deficiency tax assessment:
>
> xxx xxx xxx
>
> 3.1.2 *Preliminary Assessment Notice (PAN).* – If after review and evaluation by the Commissioner or his duly authorized representative, as the case may be, it is determined that there exists sufficient basis to assess the taxpayer for any deficiency tax or taxes, **the said Office shall issue to the taxpayer a Preliminary Assessment Notice (PAN) for the proposed assessment, <u>showing in detail, the facts and the law, rules and regulations, or jurisprudence on which the proposed assessment is based</u>** (see illustration in ANNEX 'A' hereof). If the taxpayer fails to respond within fifteen (15) days from date of receipt of the PAN, he shall be considered in default, in which case, a formal letter of demand and assessment notice shall be caused to be issued by the said Office, calling for payment of the taxpayer's deficiency tax liability, inclusive of the applicable penalties.

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[37] SUBJECT: Implementing the Provisions of the National Internal Revenue Code of 1997 Governing the Rules on Assessment of National Internal Revenue Taxes, Civil Penalties and Interest and the Extra-Judicial Settlement of a Taxpayers Criminal Violation of the Code Through Payment of a Suggested Compromise Penalty

xxx xxx xxx." *(Emphases and underscoring ours)*

On the basis of the foregoing provisions, one of the due process requirements in the issuance of a deficiency tax assessment is the issuance of a PAN.

In *Commissioner of Internal Revenue vs. Avon Products Manufacturing, Inc., et seq.,*[38] the Supreme Court said:

> "**Tax assessments issued in violation of the due process rights of a taxpayer are null and void. While the government has an interest in the swift collection of taxes, the Bureau of Internal Revenue and is officers and agents cannot be overreaching in their efforts, but must perform their duties in accordance with law, with their own rules of procedure, and always with regard to the basic tenets of due process.**
>
> **The 1997 National Internal Revenue Code, also known as the Tax Code, and revenue regulations allow a taxpayer to file a reply or otherwise submit comments or arguments with supporting documents at each stage in the assessment process. Due process requires the Bureau of Internal Revenue to consider the defenses and evidence submitted by the taxpayer and to render a decision based on these submissions. Failure to adhere to these requirements constitutes a denial of due process and taints the administrative proceedings with invalidity.**
>
> xxx xxx xxx
>
> **The importance of providing taxpayer with adequate written notice of his or her tax liability is undeniable. Under Section 228, it is explicitly required that the taxpayer be informed in writing of the law and of the facts on which the assessment is made; otherwise, the assessment shall be void. Section 3.1.2 of Revenue Regulation No. 12-99 requires the Preliminary Assessment Notice to show in detail the facts and law, rules and regulations, or jurisprudence on which the proposed assessment is based. Further, Section 3.1.4 requires the Final Letter of Demand must state the facts and law on which it is based; otherwise, the Final Letter of Demand and Final Assessment Notices themselves shall be void.** xxx.
>
> **'The use of the word 'shall' in Section 228 of the [National Internal Revenue Code] and in [Revenue**

[38] G.R. Nos. 201398-99 and 201418-19, October 3, 2018.

Regulations] No. 12-99 indicates that the requirement of informing the taxpayer of the legal and factual bases of the assessment and the decision made against him [or her] is mandatory.' <u>This is an essential requirement of due process and applies to the Preliminary Assessment Notice,</u> Final Letter of Demand with the Final Assessment Notices, and the Final Decision on Disputed Assessment.

xxx xxx xxx

The Commissioner's total disregard of due process rendered the identical Preliminary Assessment Notice, Final Assessment Notice, and Collection Letter null and void, and of no force and effect.

This Court has, in several cases, declared void any assessment that failed to strictly comply with the due process requirements set forth in Section 228 of the Tax Code and Revenue Regulation No. 12-99.

In *Commissioner of Internal Revenue v. Metro Star Superama, Inc.*,[39] this Court held that **<u>failure to send a Preliminary Assessment Notice stating the facts and the law on which the assessment was made as required by Section 228 of the Tax Code rendered the assessment made by the Commissioner as void</u>**. This Court explained:

> Indeed, Section 228 of the Tax Code clearly requires that the taxpayer must first be informed that he is liable for deficiency taxes through the sending of a PAN. He must be informed of the facts and the law upon which the assessment is made. The law imposes a substantive, not merely a formal requirement. To proceed heedlessly with tax collection without first establishing a valid assessment is evidently violative of the cardinal principle in administrative investigations – that taxpayers should be able to present their case and adduce supporting evidence. (Citation omitted)

xxx xxx xxx

In *Pilipinas Shell Petroleum Corporation v. Commissioner of Internal Revenue*,[40] this Court ruled, among others, that **the taxpayer was deprived of due process when the Commissioner <u>failed to issue</u>** a notice of informal conference and **<u>a Preliminary Assessment Notice as required by Revenue Regulation No. 12-99, in relation to Section 228 of the Tax Code</u>. Hence, the assessment was void.** 𝒥𝓇

[39] 652 Phil. 172 (2010) [Per J. Mendoza, Second Division]
[40] 565 Phil. 613 (2007) [Per J. Velasco, Jr., Second Division].

> **Compliance with strict procedural requirements must be followed in the collection of taxes** as emphasized in *Commissioner of Internal Revenue v. Algue, Inc.*:[41]
>
> > Taxes are the lifeblood of the government and so should be collected without unnecessary hindrance. On the other hand, **such collection should be made in accordance with law as any arbitrariness will negate the very reason for government itself.** It is therefore necessary to reconcile the apparently conflicting interests of the authorities and the taxpayers so that the real purpose of taxation, which is the promotion of the common good, may be achieved.
> >
> > xxx xxx xxx
> >
> > **But 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. If it is not, then the taxpayer has a right to complain and the courts will then come to his succor. <u>For all the awesome power of the tax collector, he may still be stopped in his tracks if the taxpayer can demonstrate...that the law has not been observed</u>.** (Emphasis supplied)
>
> xxx. ***<u>[The Commissioner of Internal Revenue's]</u>*** **<u>disregard of the standards and rules renders the deficiency tax assessments null and void</u>.** xxx." *(Emphases and underscoring ours)*

The foregoing doctrinal pronouncements affirms as part of the due process requirements in the issuance of tax assessments is that the taxpayer must be informed in writing of the law and of the facts on which the assessment is made. Such requirement must be embodied not only in the Final Demand Letter (with the FAN), **but also in the PAN**. In case respondent or the BIR fails to observe, *inter alia*, the said requirement, it shall have the effect of rendering the corresponding deficiency tax assessment void, and of no force and effect, since such failure violates the due process rights of the concerned taxpayer.

Considering that in this case, there is no showing that a PAN has been issued against petitioner, indicating the law and of the facts

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[41] 241 Phil. 829 (1988) [Per J. Cruz, First Division].

on which the proposed assessment is made, the subject deficiency income tax is void.

At any rate, there is still yet another ground which renders the subject income tax assessment a nullity.

The subject income tax assessment is void since petitioner's tax liability remains indefinite.

Petitioner likewise stresses that that the FAN dated January 24, 2011 did not set and fix the tax liability, which is still subject to modification of adjustment, rendering it legally infirm.

We agree with petitioner.

In *Commissioner of Internal Revenue vs. Fitness By Design, Inc.* ("*Fitness By Design* case"),[42] the Supreme Court said:

> "**The issuance of a <u>valid</u> formal assessment is a substantive prerequisite for collection of taxes.** Neither the National Internal Revenue Code nor the revenue regulations provided for a 'specific definition or form of an assessment.' However, the National Internal Revenue Code defines its explicit functions and effects. **An assessment does not only include a computation of tax liabilities; it also includes a demand for payment within a period prescribed. <u>Its main purpose is to determine the amount that a taxpayer is liable to pay</u>.**
>
> xxx xxx xxx
>
> **The disputed Final Assessment Notice is not a valid assessment.**
>
> **...it lacks the definite amount of tax liability for which respondent is accountable. It does not purport to be a demand for payment of tax due, which a final assessment notice should supposedly be. An assessment, in the context of the National Internal Revenue Code, is a 'written notice and demand made by the [Bureau of Internal Revenue] on the taxpayer for the settlement of a tax liability that is there definitely set and fixed.' Although the disputed notice provides for the computation of respondent's tax liability, <u>the amount remains indefinite</u>.**

[42] G.R. No. 215957, November 9, 2016.

> **It only provides that the tax due is still subject to modification, depending on the date of payment.** Thus:
>
> > The complete details covering the aforementioned discrepancies established during the investigation of this case are shown in the accompanying Annex 1 of this Notice. The 50% surcharge and 20% interest have been imposed pursuant to Sections 248 and 249 (B) of the [National Internal Revenue Code], as amended. **Please note, *however, that the interest and the total amount due will have to be adjusted if prior or beyond April 15, 2004.*** (Emphasis Supplied)
> >
> > xxx xxx xxx
>
> xxx. **The total amount depended upon when respondent decides to pay. The notice, therefore, did not contain a definite and actual demand to pay.**
>
> Compliance with Section 228 of the National Internal Revenue Code is a substantive requirement. It is not a mere formality. Providing the taxpayer with the factual and legal bases for the assessment is crucial before proceeding with tax collection. **Tax collection should be premised on a valid assessment,** which would allow the taxpayer to present his or her case and produce evidence for substantiation." *(Emphases and underscoring ours)*

Based on the foregoing, to be valid, a tax assessment must not only contain a computation of tax liabilities, it must also include a demand upon the taxpayer for the settlement of a tax liability that is there <u>definitely set and fixed</u>.

A careful scrutiny of the subject FAN dated January 24, 2011,[43] reveals that just as in the *Fitness by Design* case, although the same FAN provides for the computation of petitioner's income tax liability, the amount thereof remains indefinite, since the tax due is still subject to modification. Specifically, the said FAN states:

> "***Please take note that <u>the interest and total amount due will have to be adjusted if paid beyond the date specified therein</u>.***" *(Emphasis and underscoring ours)*

Furthermore, it is noteworthy that the same statements are found in the FDDA dated August 10, 2012.[44] In addition, it is not

[43] Exhibit "P-3", Docket – Vol. I, at p. 296.
[44] Exhibit "P-5", Docket – Vol. I, at p. 318.

clear as to which does the phrase *"the date specified therein"* actually refer. In view of this vagueness, the indefiniteness in the amount being assessed becomes even more apparent.

Correspondingly, the subject FAN and the assessment made in the FDDA dated August 10, 2012, hardly fall under the jurisprudential definition of a tax assessment under the NIRC, considering that they lack *"a due tax liability that is there definitely set and fixed."* They likewise do not purport to be demands for payment of tax due, which a final assessment notice should supposedly be. Clearly, the subject tax assessment is void, and thus, bear no valid fruit.[45]

Petitioner is not liable to pay the subject compromise penalty.

Since the subject income tax assessment is void, as above shown, petitioner cannot likewise be held liable to the compromise penalty in the amount of ₱25,000.00. Nevertheless, it must be stressed that a compromise is, by its nature, mutual in essence.[46] It implies agreement. One party cannot impose it upon the other.[47] Compromise penalties are only amounts suggested in settlement of criminal liability and may not be imposed or exacted on the taxpayer in the event of refusal to pay the suggested amount.[48] Considering that there is no indication that petitioner consented to the subject compromise penalty, the said amount cannot be sustained.

In view of the finding that the subject assessment is invalid and the subject compromise penalty may not be imposed in this case, it becomes unnecessary to address the other issues and respective arguments raised by the parties.

WHEREFORE, in light of the foregoing considerations, the instant *Petition for Review* is **GRANTED**. Accordingly, the assailed *Final Decision* holding petitioner liable for income tax for taxable year 2007 in the total amount of ₱22,640,164.15, inclusive of interest and

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[45] *Commissioner of Internal Revenue vs. Pilipinas Shell Petroleum Corporation*, G.R. Nos. 197945 and 204119-20, July 9, 2018, G.R. No.197945 citing *Commissioner of Internal Revenue vs. Reyes*, G.R. Nos. 159694 and 163581, January 27, 2006.
[46] Refer to *Vda. De San Agustin vs. Commissioner of Internal Revenue*, G.R. No. 138485, September 10, 2001.
[47] *Commissioner of Internal Revenue vs. Abad, et al.*, G.R. No. L-19627, June 27, 1968.
[48] Refer to Part III.4, Revenue Memorandum Order No. 7-2015.

surcharge, is **WITHDRAWN and SET ASIDE**. Moreover, the FAN dated January 24, 2011 and FDDA dated August 10, 2012 are **CANCELLED** and **SET ASIDE**.

SO ORDERED.

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Associate Justice

WE CONCUR:

Cielito N. Mindaro-Grulla
CIELITO N. MINDARO-GRULLA
Associate Justice

JEAN MARIE A. BACORRO-VILLENA
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.
JUANITO C. CASTAÑEDA, JR.
Associate Justice
Chairperson

CERTIFICATION

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

ROMAN G. DEL ROSARIO
Presiding Justice