

REPUBLIC OF THE PHILIPPINES
Court of Tax Appeals
QUEZON CITY

Third Division

NEXT MOBILE, INC.,

Petitioner,

CTA CASE NO. 8516

Members:

-versus-

*Bautista, Chairperson
Fabon-Victorino, and
Ringpis-Liban, JJ.*

COMMISSIONER OF INTERNAL
REVENUE,

Respondent.

Promulgated:

OCT 14 2015

Case 1:00 p.m.

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DECISION

BAUTISTA, J:

The Case¹

This is a Petition for Review filed on July 13, 2012, pursuant to Section 7(a)(1)² of Republic Act ("RA") No. 1125³, as amended by RA No. 9282⁴ and RA No. 9503⁵, seeking for the Court to nullify the Final Decision of respondent for payment of deficiency income tax, interest and compromise penalty against petitioner for taxable year 2006 in the

¹ Records, CTA Case No. 8516, pp. 6 and 24.

² Sec. 7. *Jurisdiction.* -The Court of Tax Appeals 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.

³ An Act Creating the Court of Tax Appeals, as amended.

⁴ An Act Expanding the Jurisdiction of the Court of Tax Appeals (CTA), Elevating its Rank to the Level of a Collegiate Court with Special Jurisdiction and Enlarging its Membership, Amending for the Purpose Certain Sections of Republic Act No. 1125, as amended, Otherwise Known as the Law Creating the Court of Tax Appeals, and for Other Purposes.

⁵ An Act Enlarging the Organizational Structure of the Court of Tax Appeals, Amending for the Purpose Certain Sections of the Law Creating the Court of Tax Appeals, and for Other Purposes.



aggregate amount of Php79,320,554.30; and to order respondent to cancel the said assessment.

The Parties⁶

Petitioner Next Mobile, Inc. is duly organized and existing under Philippine laws, with principal address at Next Mobile Building, 2244 España Avenue, Sampaloc, Manila.

Respondent Commissioner of Internal Revenue ("CIR") is the government authority designated to collect all taxes, grant refunds, issue and abate assessments, and examine books of accounts and returns filed with it to determine the correctness of taxes paid under the 1997 National Internal revenue Code ("NIRC").

The Facts

As stated in the Joint Stipulation of Facts and Issues ("JSFI")⁷ filed by registered mail on October 19, 2012, the factual antecedents of this case are as follows:

3. Next Mobile is authorized to construct, establish, operate and maintain radio paging systems and mobile communications services, and to install and operate corresponding radio transmitting and receiving stations and communication facilities in or outside the Philippines.

4. On 27 April 2007, Next Mobile filed its Annual Income Tax Return or accomplished BIR Form 1702 ("2006 ITR") for taxable year 2006 with the Bureau of Internal Revenue ("BIR").

5. On 21 September 2007, Next Mobile received a letter of authority 00000367 dated 18 September 2007 together with a "First Request for Presentation of Records" ("LOA 00000367") for the examination of Next Mobile's books of accounts and other accounting records for all internal revenue taxes for taxable year 2006.

⁶ *Id.*, Joint Stipulation of Facts and Issues ("JSFI"), pp. 152-159.

⁷ *Id.*

6. On 9 October 2007, Next Mobile received the Second Request for Presentation of Records dated 27 September 2007 ("Second Request").

7. On 15 October 2007, Next Mobile, through a letter dated 14 October 2007 ("14 October 2007 Letter"), requested for an extension of time or until 15 November 2007, within which to submit the required books of accounts in the Second Request in view of the examination being conducted by Next Mobile's external auditors of the said books of accounts.

8. On 16 October 2007, Next Mobile received the Final Request for Presentation of Records dated 10 October 2007 ("Final Request").

9. On 19 February 2008, Next Mobile received the Summons and/or *Subpoena Duces Tecum* dated 11 February 2008 ("Subpoena").

10. On 29 February 2008, Next Mobile, in a letter dated 29 February 2008 ("29 February 2008 Letter"), submitted to the Regional Director, all the documents listed in the *Subpoena*.

11. On 4 May 2009, Next Mobile received a Notice of Informal Conference dated 30 April 2009 ("Notice of Informal Conference") from Respondent through Revenue District Office No. 32 ("RDO 32").

12. On 30 July 2009, Next Mobile received a Revised Post Reporting Notice dated 29 July 2009 ("Revised Post Reporting Notice") from Respondent through RDO 32.

13. On 6 April 2010, Next Mobile received from Respondent, through Regional Director of Revenue Region No. 6 ("Regional Director"), a Preliminary Assessment Notice dated 25 March 2010 ("PAN") for deficiency income tax and compromise penalty allegedly due for CY 2006.

14. On 15 April 2010, Next Mobile received from Respondent, through Regional Director, a formal letter of

demand [("FLD")] with final assessment notice dated 14 April 2010 ("FAN") for the deficiency income tax, inclusive of interest, and compromise penalty in the aggregate amount of P 79,298,554.30 ("Deficiency Tax Assessment").

15. On 14 May 2010, Next Mobile filed a written protest dated 13 May 2010 ("Protest") to the FAN.

16. On 8 June 2010, Respondent, through Regional Director, issued a letter: (1) informing Next Mobile that the entire docket of the case, including the protest, was forwarded to RDO 32; and (ii) instructing Next Mobile to address all communications to RDO 32 ("8 June 2010 Letter").

17. On 11 June 2010, RDO 32 issued a tax verification notice authorizing Revenue Officers Dionisio Cruz, Jr. under Group Supervisor Alemar Sani to handle the internal revenue taxes of Next Mobile for taxable year 2006 which was the subject of the Protest.

18. On 13 June 2012, Next Mobile received a letter dated 08 June 2012 from the Regional Director ("[Final Decision]") reiterating the Deficiency Tax Assessment and requesting for the payment of the same, otherwise, the case will be forwarded to the Collection Division of Revenue Region No. 6.

19. On 6 July 2012, Next Mobile, through the undersigned, sent a letter dated 5 July 2012 to the Regional Director ("5 July 2012 Letter") stating that Next Mobile would treat the 8 June 2012 Letter as the Respondent's final decision on the Protest unless Next Mobile receives a written communication, on or before 13 July 2012, clarifying that the re-investigation would continue.

20. On 13 July 2012, Next Mobile filed the instant Petition for Review assailing the Deficiency Tax Assessment.

21. On 31 July 2012, Next Mobile received a letter dated 27 July 2012 from the Regional Director (27 July 2012 Letter") informing Next Mobile that the docket of the case

was forwarded to the Collection Division of Revenue Region No. 6.

22. The following documents are authentic and duly executed:

- a. 2006 ITR;
- b. LOA 00000367;
- c. Second Request;
- d. Next Mobile's 14 October 2007 Letter;
- e. Final Request;
- f. *Subpoena*[;]
- g. Next Mobile's 29 February 2008 Letter;
- h. Notice of Informal Conference;
- i. Revised Post Reporting Notice;
- j. PAN;
- k. FAN;
- l. Protest;
- m. 8 June 2010 Letter;
- n. [Final Decision];
- o. Audit Report on Income Tax for taxable year 2006;
- p. Audit Report on Income Tax-MCIT for taxable year 2006;
- q. Next Mobile's 5 July 2012 Letter;
- r. 27 July 2012 Letter addressed to Next Mobile;

On August 31, 2012, respondent filed her Answer,⁸ interposing the following Special and Affirmative Defenses:

14. **RESPONDENT** hereby adopts by way of reference all of the allegations in the foregoing paragraphs insofar as the same are material and relevant, and alleges that:

The subject assessment has become final and executory; hence, not appealable to this Honorable Court.

15. Under Section 228 of the Tax Code of 1997, as amended, a tax assessment may be administratively protested by filing a request for reinvestigation or reconsideration within 30 days from receipt of due assessment notice. Within sixty (60) days from the filing of the protest, all relevant supporting documents shall have been submitted; otherwise, the assessment shall become final;

16. In the instant case, while a protest on the assessment was indeed filed on 14 May 2010, the subject taxpayer, however, failed to submit "*relevant supporting documents*" in support of its protest. A thorough perusal of the records of the case would show that the subject taxpayer merely submitted "schedules" of its claimed expenses and not "*relevant supporting documents*" as clearly required by law;

17. Therefore, considering that the subject taxpayer failed to submit documents in support of its protest, the Final Assessment Notice No. 30-06-IT0071 it received on 14 May 2010 has become final, executory and demandable. Accordingly, the said assessment ceases to be a disputed assessment and thus, the legality and validity thereof can no longer be the subject of a judicial inquiry in the instant Petition for Review (*La Flor Dela Isabela, Inc. vs. CIR, CTA Case No. 7709, 09 June 2010*);



⁸ *Id.*, Records, pp. 58-61.

18. Moreover, without conceding to the claim that the subject assessment had attained finality, respondent respectfully submits that her letter dated 8 June 2012 addressed to the subject taxpayer cannot, in any way, be considered as a Final Decision which is appealable to this Honorable Court pursuant to its jurisdiction provided under Section 7 of Republic Act No. 1125, as amended;

19. Contrary to the claim of the petitioner, the respondent's letter dated 8 June 2012 is neither a demand letter nor a collection letter so as to [be considered] as a Final Decision of the respondent on the protest. Rather, said letter is a mere statement of the consequence of the failure to comply with the requirements to submit supporting documents within the 60-day period. Accordingly, the Honorable Court has no jurisdiction to entertain the instant Petition.

Procedural due process has been complied with in the issuance of the assessment.

20. Verily, under existing rules and regulations, a final assessment notice (FAN) shall be issued after the taxpayer filed or failed to file a reply to the preliminary assessment notice within 15 days from receipt thereof (*Revenue Regulations Nos. 12-85 and 12-99 and Revenue Memorandum Order No. 37-94*);

21. However, it should be noted that the FAN in the instant case was not issued in total disregard of the right of the subject taxpayer to file a reply to the Preliminary Assessment Notice (PAN). Records show that the PAN was sent through mail to the subject taxpayer as early as 25 March 2010. After the lapse of sufficient period of time from the mailing of the PAN, it may be reasonably presumed that the subject taxpayer has received the PAN;

22. More importantly, it should be emphasized that a PAN is not indispensable and the issuance thereof may be dispensed with. In fact, the subject taxpayer is not obliged to protest the PAN and failure on its part to file a reply thereto will not result in the finality of the assessment. What the law requires is the issuance of FAN



which is in substantial compliance of what is mandated under Sec. 228 of the National Internal Revenue Code of 1997, as amended. (*BPI vs. CIR*, CTA Case No. 7397, 09 April 2008 and *Direct Container Line Phils., Inc. vs. CIR*, CTA Case No. 7676, 70 September 2009);

23. In the case of *Commissioner of Internal Revenue vs. Menguito*, GR No. 167560, 17 September 2008, the Supreme Court elucidated the indispensability of the PAN, thus:

"It should be emphasized that the stringent requirement that an assessment notice be satisfactorily proven to have been issued and released, or if receipt thereof is denied, that said assessment notice have been served [on] the taxpayer, applies only to formal assessments prescribed under Section 228 of the NIRC, but not to post-reporting notices or pre-assessment notices. [sic] A post-reporting notices or pre-assessment notices do not bear the gravity of a formal assessment notice. The post-reporting notice or pre-assessment notice merely hint at the initial findings of the BIR against a taxpayer and invites the latter to an "informal" conference or clarificatory meeting. Neither notice contains a declaration of the tax liability of the taxpayer or a demand for payment thereof. Hence, the lack of such notices inflicts no prejudice on the taxpayer for as long[] as the latter is properly served a formal assessment notice." (emphasis and underscoring supplied)

24. In the instant case, while the subject taxpayer was not able to respond to the PAN, it was, nevertheless, duly served with the PAN dated 25 March 2010. In fact, the subject taxpayer was not denied due process and no prejudice was inflicted against it because of the protest filed on 14 May 2010. Accordingly, its failure to file a reply to the PAN shall not be deemed as a deprivation of its right to procedural due process.

Petitioner has the burden of showing the incorrectness of the subject assessment.

25. The subject assessment is valid and correct and the petitioner has the burden of proof to impugn its validity (*Behn Meyer & Co. vs. Collector of Internal Revenue*, 27 Phil. 647). Thus, similarly held, tax assessments by examiners are presumed correct and made in good faith and the taxpayer has the duty to prove otherwise (*Commission of Internal Revenue vs. Construction Resources of Asia, Inc.*, 145 SCRA 671); and assessments duly made by the BIR examiner and approved by her superior officers will not be disturbed (*Gutierrez vs. Villegas*, 8 SCRA 547);

26. 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]);

27. All presumptions are in favor of the correctness of the assessment made by the Commissioner of Internal Revenue; the taxpayer must prove the contrary (*Commissioner of Internal Revenue vs. Antonio Tuason, Inc.* 173 SCRA 397; *Commissioner of Internal Revenue vs. Construction Resources of Asia, Inc.*, 145 SCRA 671);

28. The assessments were issued in the regular course and within the reglementary period to assess provided by law.

Respondent and petitioner filed their respective Pre-trial Briefs⁹ on September 21, 2012 and September 24, 2012.

On October 19, 2012, the parties filed their JSFI¹⁰ by registered mail, and thus a Pre-Trial Order¹¹ was issued on November 16, 2012.

⁹ *Id.*, pp. 84-90 and 91-102.

¹⁰ *Id.*, JSFI, pp. 152-159.

¹¹ *Id.*, pp. 176-184.

On August 22, 2013, petitioner filed its Formal Offer of Evidence,¹² to which respondent filed her Comment¹³ on September 9, 2013.

On October 1, 2013, the Court resolved¹⁴ petitioner's Formal Offer of Evidence, which was questioned by petitioner in its Motion for Partial Reconsideration¹⁵ dated October 29, 2013. There being no comment on the part of respondent, the Court issued a resolution¹⁶ thereon on January 14, 2014.

On June 9, 2014, respondent filed her Formal Offer of Documentary Evidence¹⁷, to which petitioner filed its Comments/Objections¹⁸ on June 30, 2014 by registered mail.

On August 26, 2014, the Court resolved¹⁹ respondent's Formal Offer of Documentary Evidence and granted the parties thirty (30) days from receipt to file their respective memorandum.

Petitioner filed its Memorandum²⁰ by registered mail on September 29, 2014, followed by Respondent's Memorandum²¹ filed on October 28, 2014.

Thus on November 3, 2014, the Court promulgated a Resolution²² submitting the case for Decision.

Hence, this Decision.

*The Issues*²³

1. WHETHER THE COURT HAS JURISDICTION TO ENTERTAIN THE INSTANT PETITION FOR REVIEW;

¹² *Id.*, pp. 852-926.

¹³ *Id.*, pp. 927-928.

¹⁴ *Id.*, pp. 955-956.

¹⁵ *Id.*, pp. 957-960.

¹⁶ *Id.*, pp. 971-972.

¹⁷ *Id.*, pp. 1045-1055, exclusive of annexes.

¹⁸ *Id.*, pp. 1147-1161.

¹⁹ *Id.*, pp. 1164-1165.

²⁰ *Id.*, pp. 1170-1196.

²¹ *Id.*, pp. 1198-1206.

²² *Id.*, p. 1208.

²³ *Id.*, JSFI, pp. 156-157.

2. WHETHER THE RIGHT OF NEXT MOBILE TO PROCEDURAL DUE PROCESS UNDER SECTION 228 OF THE 1997 NIRC AND REVENUE REGULATIONS NO. 12-99 WAS VIOLATED WHEN RESPONDENT ISSUED THE FAN AND THE JUNE 8, 2012 LETTER.

3. WHETHER THE FAN HAS BECOME FINAL AND DEMANDABLE;

4. WHETHER RESPONDENT INDICATED IN THE FAN THE FACTS AND LAW WHY PETITIONER DID NOT INCUR AN OPERATING LOSS FOR CY 2006;

5. WHETHER THE DEFICIENCY TAX ASSESSMENT HAS FACTUAL AND LEGAL BASES; AND

6. WHETHER PETITIONER IS LIABLE TO PAY THE DEFICIENCY TAX ASSESSMENT.

Petitioner's arguments

Petitioner avers that the Court has jurisdiction to entertain the suit since respondent's letter dated June 8, 2012 is the decision appealable to the Court under Section 228 of the 1997 NIRC; that the assessment is not final, executory and unappealable as petitioner submitted all relevant documents in support of its protest; that the FAN and Final Decision were issued in violation of petitioner's right to procedural due process under Section 228 of the 1997 NIRC and Revenue Regulations ("RR") No. 12-99; that the tax assessments have no factual and legal bases since petitioner properly substantiated the expenses claimed as deductions and that the questioned expenses were either properly subjected to or exempt from withholding tax; that petitioner's taxable income was at a loss and not at the amount of zero, as claimed by respondent; that adding back of the net loss is void for being a wholesale disallowance of petitioner's expenses; and that petitioner is not liable for any compromise penalty for it did not consent to the said imposition.

Respondent's Counter-Arguments

Respondent claims that the subject assessment is final and executory; that procedural due process has been complied with in the issuance of the deficiency assessment; and that the assessment provides the factual and legal bases required.

The Ruling of the Court

The Court finds partial merit in the Petition for Review.

The Court has jurisdiction to entertain the present Petition for Review since the assessment has not yet attained finality.

Respondent claims that the assessment has attained finality due to petitioner's non-compliance with *Section 228 of the 1997 NIRC* for failure to present relevant supporting documents in relation to its protest. Hence, the assessment may not anymore be questioned before this Court.

A cursory reading of the relevant portions of *Section 228 of the 1997 NIRC* should shed light on this issue, as follows:

SECTION 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 preassessment notice shall not be required in the following cases: xxx

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 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.

The above provision provides the remedy to dispute a tax assessment within a certain period of time. It states that an assessment may be protested by filing a request for reconsideration or reinvestigation within thirty (30) days from receipt of the assessment by the taxpayer. Within sixty (60) days from filing of the protest, all relevant supporting documents shall have been submitted; otherwise, the assessment shall become final. Should the protest be denied, it may be appealed to the CTA within thirty (30) days from receipt of said denial.

In the case of *Commissioner of Internal Revenue v. First Express Pawnshop Company Inc.*²⁴, the Supreme Court explained that "relevant supporting documents" are those documents necessary to support the legal basis in disputing a tax assessment, as determined by the taxpayer. The BIR can only inform the taxpayer to submit additional documents but cannot demand what type of supporting documents should be submitted.²⁵ Otherwise, a taxpayer will be at the mercy of the BIR, which may require the production of documents that a taxpayer cannot submit.²⁶ Thus, petitioner may choose to submit the

²⁴ G.R. Nos. 172045-46, June 16, 2009, 589 SCRA 253.

²⁵ *Id.*

²⁶ *Id.*

protest even with no supporting documents without invalidating its protest.²⁷ The lack of documentation will only matter in the BIR's evaluation of the merits of the said protest, but should not result in the finality of the deficiency assessment.²⁸

Records reveal that petitioner received the FAN²⁹ on April 15, 2010 and it had until May 17, 2010 to submit its protest since May 15, 2010 falls on a Saturday. On May 14, 2010, petitioner filed its Protest.³⁰ Hence, petitioner has sixty (60) days from the filing of the said protest or until July 13, 2010, to submit relevant supporting documents, only if it chooses to do so.

Petitioner has complied with the requisites in disputing an assessment pursuant to *Section 228 of the 1997 NIRC* and *RA No. 1125* since it filed its protest three days before due date. Whether or not it submitted additional documents to prove its claim does not have a detrimental effect on its protest.

On the issue of jurisdiction, *Section 7 of RA No. 1125*³¹, as amended, grants the CTA the exclusive appellate jurisdiction to review the decisions of respondent in cases involving disputed assessments, fees or other charges, and penalties in relation thereto, or other matters arising under the 1997 NIRC. Further, *Section 11 of RA No. 1125*³²

²⁷ *Phil Foods Properties, Inc. v. Commissioner of Internal Revenue*, CTA Case Nos. 8185 & 8238, December 3, 2014.

²⁸ *Id.*

²⁹ *Records*, p. 1083.

³⁰ *Records*, pp. 1058-1067.

³¹ *SECTION 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

³² *SECTION 11. Who May Appeal; Mode of Appeal; Effect of Appeal.* –

Any party adversely affected by a decision, ruling or inaction of the Commissioner of Internal Revenue, the Commissioner of Customs, the Secretary of Finance, the Secretary of Trade and Industry or the Secretary of Agriculture or the Central Board of Assessment Appeals or the Regional Trial Courts may file an appeal with the CTA within thirty (30) days after the receipt of such decision or ruling or after the expiration of the period fixed by law for action as referred to in Section 7(a)(2) herein.

Appeal shall be made by filing a petition for review under a procedure analogous to that provided for under Rule 42 of the 1997 Rules of Civil Procedure with the CTA within thirty (30) days from the receipt of the decision or ruling or in the case of inaction as herein provided, from the expiration of the period fixed by law to act thereon. A Division of the CTA shall hear the appeal: Provided, however, That with respect to decisions or rulings of the Central Board of Assessment Appeals and the Regional Trial Court in the exercise of its appellate jurisdiction appeal shall be made by filing a petition for review under a procedure analogous to that provided for under Rule 43 of the 1997 Rules of Civil Procedure with the CTA xxx



provides that any taxpayer adversely affected by a decision of the CIR may file an appeal with the CTA within thirty (30) days after the receipt of such decision.

It is undisputed that on June 13, 2012, petitioner received the Final Decision of respondent dated June 8, 2012 on its protest, reiterating the assessment and requesting for payment of the alleged deficiency taxes stated therein.³³ Therefore, it has until July 13, 2012 to file its appeal with the Court. Thus, on July 13, 2012, petitioner timely filed its Petition for Review³⁴.

On the basis of the foregoing, the tax assessment cannot be considered as final, executory and demandable; and the petitioner was correct in filing the present Petition for Review with the Court, which in turn, has jurisdiction to entertain the same.

Petitioner's right to procedural due process was not violated by respondent when the latter issued the FAN ahead of the former's protest to the PAN.

Petitioner argues that the FAN was issued in violation of its right to procedural due process under *Section 228 of the 1997 NIRC* and *Revenue Regulations No. 12-99*.

One of the most basic and fundamental precepts of law enshrined in the Constitution is that no person shall be deprived of his property without due process of law.³⁵ The concept of due process in tax assessments can be found in *Section 228 of the 1997 NIRC* and *Section 3 of RR No. 12-99*.

The previously-stated *Section 228 of the 1997 NIRC* provides that if the CIR finds that proper taxes should be assessed, the taxpayer shall be notified of the finding through a PAN. On the other hand, *Section 3 of RR No. 12-99*, states the detailed process which assessments should undergo to ensure that the taxpayer is accorded due process, to wit:

³³ *Records, JSFI*, p. 155.

³⁴ *Id.*, pp. 6-29.

³⁵ Article III, Section 1: "No person shall be deprived of life, liberty, or property without due process of law, nor shall any person be denied the equal protection of the laws."

SECTION 3. *Due Process Requirement in the Issuance of a Deficiency Tax Assessment.* —

3.1 Mode of procedures in the issuance of a deficiency tax assessment:

3.1.1 *Notice for informal conference.* — The Revenue Officer who audited the taxpayer's records shall, among others, state in his report whether or not the taxpayer agrees with his findings that the taxpayer is liable for deficiency tax or taxes. If the taxpayer is not amenable, based on the said Officer's submitted report of investigation, the taxpayer shall be informed, in writing, by the Revenue District Office or by the Special Investigation Division, as the case may be (in the case Revenue Regional Offices) or by the Chief of Division concerned (in the case of the BIR National Office) of the discrepancy or discrepancies in the taxpayer's payment of his internal revenue taxes, for the purpose of "Informal Conference," in order to afford the taxpayer with an opportunity to present his side of the case. If the taxpayer fails to respond within fifteen (15) days from date of receipt of the notice for informal conference, he shall be considered in default, in which case, the Revenue District Officer or the Chief of the Special Investigation Division of the Revenue Regional Office, or the Chief of Division in the National Office, as the case may be, shall endorse the case with the least possible delay to the Assessment Division of the Revenue Regional Office or to the Commissioner or his duly authorized representative, as the case may be, for appropriate review and issuance of a deficiency tax assessment, if warranted.

3.1.2 *Preliminary Assessment Notice (PAN).* — If after review and evaluation by the Assessment Division or 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, at least by registered mail, a Preliminary Assessment Notice (PAN) for the proposed assessment, showing in detail, the



facts and the law, rules and regulations, or jurisprudence on which the proposed assessment is based (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.

3.1.3 *Exceptions to Prior Notice of the Assessment.* – The notice for informal conference and the preliminary assessment notice shall not be required in any of the following cases, in which case, issuance of the formal assessment notice for the payment of the taxpayer's deficiency tax liability shall be sufficient:

- (i) When the finding for any deficiency tax is the result of mathematical error in the computation of the tax appearing on the face of the tax return filed by the taxpayer; or
 - (ii) When a discrepancy has been determined between the tax withheld and the amount actually remitted by the withholding agent; or
 - (iii) 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
 - (iv) When the excise tax due on excisable articles has not been paid; or
 - (v) When an 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.

3.1.4 Formal Letter of Demand and Assessment Notice. — The formal letter of demand and assessment notice shall be issued by the Commissioner or his duly authorized representative. The letter of demand calling for payment of the taxpayer's deficiency tax or taxes shall state the facts, the law, rules and regulations, or jurisprudence on which the assessment is based, otherwise, the formal letter of demand and assessment notice shall be void (see illustration in ANNEX B hereof). The same shall be sent to the taxpayer only by registered mail or by personal delivery. If sent by personal delivery, the taxpayer or his duly authorized representative shall acknowledge receipt thereof in the duplicate copy of the letter of demand, showing the following: (a) His name; (b) signature; (c) designation and authority to act for and in behalf of the taxpayer, if acknowledged received by a person other than the taxpayer himself; and (d) date of receipt thereof.

The above clearly provides the procedures to be undertaken by revenue officers in the issuance of a deficiency assessment. As stated therein, the taxpayer is given a fifteen (15)-day period from receipt of the PAN within which to reply. Failure to reply would make the taxpayer in default, and a FAN and FLD shall be issued.

In the case at bar, the PAN was issued on March 25, 2010 and received by petitioner on April 6, 2010³⁶. On April 15, 2010, petitioner received the FAN dated April 14, 2015.³⁷ Then on May 14, 2010, petitioner filed its protest to the FAN.³⁸

While it is true that respondent did not await the lapse of the fifteen (15)-day period before the latter issued the FAN and FLD, the requirements for procedural due process under *RR No. 12-99* were substantially complied with.

³⁶ *Records, JSFI*, p. 154; pp. 1079-1081; *Exhibit "GG."*

³⁷ *Id.*, p. 154; p. 1083.

³⁸ *Id.*, p. 154

A Notice of Informal Conference³⁹ was received by petitioner on May 4, 2009 and in compliance with such notice, petitioner's representatives met with Ms. Alma Cayabyab on May 8, 2009.⁴⁰ The purpose of the Informal Conference is to afford the taxpayer with an opportunity to present his side of the case. Thus, at that stage, petitioner was already given the opportunity to rebut the findings of the BIR.

It must be noted that a protest against the PAN is not indispensable, unlike the protest against the FAN, and the fact of non-protest shall not, in any way, make the former final and unappealable.⁴¹ While the FAN was issued ahead of the fifteen (15)-day period, it inflicts no prejudice on petitioner, as long as the latter was properly served such FAN and that it was able to intelligently contest the FAN by filing a protest letter within the period provided by law.⁴² In the case of *International Exchange Bank v. Commissioner of Internal Revenue*⁴³, the Supreme Court upheld the decision of the CTA *En Banc* in affirming the decision of the CTA Division in ruling that the taxpayer was accorded procedural due process even if the FAN was issued prior to the expiration of the fifteen (15)-day period to respond to the PAN.

Therefore, the mere fact that petitioner received the FAN even before it had the opportunity to respond to the PAN is no basis for the claim of deprivation of due process since petitioner was given ample opportunity to explain itself through its meetings with BIR personnel, and it protests to the PAN as well as to the FAN.

**The deficiency tax assessment has
factual and legal bases.**

As provided in the previously-cited *Section 228 of the 1997 NIRC*, taxpayers shall be informed in writing of the law and the facts on which the assessment is made, failure to do so shall render the said assessment void.)

³⁹ *Id.*, p. 154; Exhibit "EE."

⁴⁰ Exhibit "EE."

⁴¹ *Global Metal Tech Corporation v. Commissioner of Internal Revenue*, CTA Case No. 8329, September 23, 2014.

⁴² *Id.*

⁴³ G.R. No. 171266, April 4, 2007, 520 SCRA 688.

An inspection of the FAN⁴⁴ issued on April 14, 2010 will reveal the breakdown of the total amount due, to be paid on or before May 17, 2010:

Tax Due	₱ 49,530,346.44
Surcharge 25%	-
Interest (up to 04/15/2010)	29,718,207.86
Compromise Penalty	50,000.00
Total Amount Due	₱ 79,298,554.30

The FLD⁴⁵ dated April 14, 2010 provided further details of the Deficiency Income Tax and Compromise Penalty, to wit:

Taxable Income per return			₱	-
Add: 50% Disallowances - sec. 6 (B), NIRC/RMC 23-2000 unsupported exp. - sec. 34 NIRC				
Purchases		₱	5,026,241.50	
Salaries/wages & Benefits - Direct Cost/OE			16,606,693.00	
Materials/supplies/facilities/rental				
<i>per</i> BIR Form 1702	₱	153,136,521.00		
Less: Rental Inc. Site Switch <i>per</i> F/S		82,222,577.00		
Materials & supplies		70,913,944.00	35,456,972.00	
Other			4,144,631.00	
Fringe Benefits			1,470,550.00	
Membership fees			25,416.50	
Repairs & Maintenance - supplies			3,735,476.00	
Office Supplies			308,798.50	
Interest expense			3,258,409.50	
Insurance			1,583,668.50	
Representation & Entertainment			1,047,274.50	
Transportation & Travel			1,663,209.50	
Communication, light & water			9,945,158.00	
Recruitment & training			465,915.50	
Administrative Expenses - others			154,041.00	
Bills processing			919,782.00	
Others			6,100,489.00	91,912,726.00
Not subjected to withholding tax - Sec. 34k, NIRC				
Commissions		₱	206,450.00	
Rental Inc. Site Switch <i>per</i> F/S	₱	82,222,577.00		
<i>per</i> 1601		48,516,682.20	33,705,894.80	
Professional fee				
<i>per</i> BIR 1702		41,028,033.00		
<i>per</i> BIR 1601		26,818,339.70	14,209,693.30	48,122,038.10

⁴⁴ Records, p. 1083.

⁴⁵ *Id.*, pp. 1084-1086.

Taxable income <i>per</i> investigation			₱ 140,034,764.10
Tax Due			49,012,167.44
Less: tax credits /payments per return		3,875,794.00	
Less: Unsupported BIR 2307	518,179.00		
To applied to succeeding year	3,875,794.00	4,393,973.00	(518,179.00)
Deficiency Income Tax Due			₱ 49,530,346.44
Add: 25% Surcharge			
20% Interest p. a. from _____ to 4/15/2010 (Sec. 249)			29,718,207.86
Compromise Penalty (sec. 254 in relation to RMO 19-2007)			50,000.00
TOTAL AMOUNT DUE & COLLECTIBLE			₱ 79,298,554.30

Compromise Penalty - sec. 250 NIRC

Non-filing of alphalist of income payments subject to withholding tax	₱ 1,000.00
Non-filing of alphalist of compensation	1,000.00
Non-filing of Quarterly Summary List of Sales	4,000.00
Non-filing of MAP	12,000.00
Non-filing of SAWT	4,000.00
TOTAL AMOUNT DUE & COLLECTIBLE	₱ 22,000.00

From the foregoing, it is evident that respondent clearly indicated the factual and legal bases of the assessment, *viz.*:

Assessment Item	Factual Basis		Legal Basis
Purchases	₱ 10,052,483.00	Tentative ITR	At 50% - Sections 6(B) and 34 of the 1997 NIRC; RMC No. 23-2000
Salaries/wages & Benefits - Direct Cost/OE	16,606,693.00	Tentative ITR	
Materials/supplies/facilities/rental	70,913,944.00	Tentative ITR; AFS	
Other	8,289,262.00	Tentative ITR	
Fringe Benefits	2,941,100.00	Tentative ITR	
Membership Fees	50,833.00	Tentative ITR	
Repairs & Maintenance - supplies	7,470,952.00	Tentative ITR	
Office Supplies	617,597.00	Tentative ITR	
Interest Expense	6,516,819.00	Tentative ITR	
Insurance	3,167,337.00	Tentative ITR	
Representation & Entertainment	2,094,549.00	Tentative ITR	
Transportation & Travel	3,326,419.00	Tentative ITR	
Communication, Light & Water	19,890,316.00	Tentative ITR	
Recruitment & Training	931,831.00	Tentative ITR	
Administrative Expenses - Others	309,082.00	Tentative ITR	
Bills Processing	1,839,564.00	Tentative ITR	
Others	12,200,978.00	Tentative ITR	
Commissions	206,450.00	Tentative ITR	Section 34(K) of the 1997 NIRC
Rental Inc. Site Switch	33,705,894.80	AFS; BIR Form 1601	
Professional Fee	14,209,693.30	Tentative ITR; BIR Form 1601	

2

Interest	29,718,207.86	Items assessed	Section 249 of the 1997 NIRC
Compromise Penalty	50,000.00	Items assessed	Section 254 of the 1997 NIRC; RMO No. 19-2007
Compromise Penalty	22,000.00	Items assessed	Section 250 of the 1997 NIRC

Hence, petitioner's claim that the assessment has no factual and legal bases has no leg to stand on.

**Petitioner is liable to pay
deficiency income tax and interest
for taxable year 2006.**

On the outset, the Court would like to emphasize two things: (1) that assessments are presumed correct and (2) the Court is not bound by the findings of the Independent Certified Public Accountant ("ICPA").

Assessments by tax examiners are presumed correct and made in good faith and the taxpayer has the duty to prove otherwise.⁴⁶ All presumptions are in favor of the correctness of tax assessments.⁴⁷ In the absence of any proof of irregularity in the performance of duties, an assessment duly made by a BIR examiner and approved by his superior officers will not be disturbed.⁴⁸ Failure to present proof of error in the assessment will justify judicial affirmation of said assessment.⁴⁹

The Court has consistently ruled that it is not bound by the findings in the ICPA Report, which is a mere tool or guide to aid the Court in the resolution of the case.⁵⁰ Therefore, the determination of the merit or the probative value of such report is still within the province of the Court, which is free to adopt or disregard, completely or partially, the findings of the ICPA.⁵¹ In fact, the Court can make its

⁴⁶ *Sy Po v. Court of Appeals*, G.R. No. L-81446, August 18, 1988, 164 SCRA 524.

⁴⁷ *Commissioner of Internal Revenue v. Bank of the Philippine Islands*, G.R. No. 134062, April 17, 2007, 521 SCRA 373.

⁴⁸ *Id.*

⁴⁹ *Commissioner of Internal Revenue v. Court of Appeals*, G.R. Nos. 104151 and 105561, March 10, 1995, 242 SCRA 289; *Delta Motors Co. v Commissioner of Internal Revenue*, CTA Case No. 3782, May 21, 1984.

⁵⁰ *The Abbas' Orchard School, Inc. v. Commissioner of Internal Revenue*, CTA Case No. 8377, November 4, 2014, citing *Stateland, Inc. v. Commissioner of Internal Revenue*, CTA Case No. 8457, November 28, 2013.

⁵¹ *Id.*

own evaluation of the documents presented during the trial in order to intelligently resolve the conflict brought before it.⁵²

A. Deficiency Income Tax - 50% Rule

Respondent's assessment on petitioner's deficiency Income Tax is based on the 50% Rule pursuant to *Section 2.4(c) of Revenue Memorandum Circular ("RMC") No. 23-00*⁵³, to wit:

2.4 Existing Revenue Procedures and Jurisprudence Governing Assessment Based on the Best Evidence Obtainable.

— Provided hereunder are the existing revenue procedures and jurisprudence governing issuance of a deficiency tax assessment based on the best evidence obtainable:

xxx

xxx

xxx

(c) Assessment Based on Estimate; 50% Rule, in Absence of Receipts to Prove Actual Amount of Expense Deduction. — The Court held in the Mariano Zamora case that, if there is a showing that expenses have been incurred but the exact amount thereof cannot be ascertained due to absence of documentary evidence, it is the duty of the BIR to make an estimate of the deduction that may be allowable in computing the taxpayer's taxable income, bearing heavily against the taxpayer whose inexactitude is of his own making. That disallowance of 50% of the taxpayer's claimed deduction is valid.

Section 34(A) of the 1997 NIRC provides the expenses which may be deducted from gross income and the substantiation requirements related thereto:

SECTION 34. Deductions from Gross Income. — Except for taxpayers earning compensation income arising from personal services rendered under an employer-employee relationship where no deductions shall be allowed under this Section other than under Subsection (M) hereof, in computing taxable income subject to income tax under

⁵² *Id.*

⁵³ November 27, 2000.

Sections 24(A); 25(A); 26; 27(A), (B) and (C); and 28(A)(1), there shall be allowed the following deductions from gross income:

(A) *Expenses.* —

(1) *Ordinary and Necessary Trade, Business or Professional Expenses.* —

(a) *In General.* — There shall be allowed as deduction from gross income all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on or which are directly attributable to, the development, management, operation and/or conduct of the trade, business or exercise of a profession, including:

(i) A reasonable allowance for salaries, wages, and other forms of compensation for personal services actually rendered, including the grossed-up monetary value of fringe benefit furnished or granted by the employer to the employee: Provided, That the final tax imposed under Section 33 hereof has been paid;

(ii) A reasonable allowance for travel expenses, here and abroad, while away from home in the pursuit of trade, business or profession;

(iii) A reasonable allowance for rentals and/or other payments which are required as a condition for the continued use or possession, for purposes of the trade, business or profession, of property to which the taxpayer has not taken or is not taking title or in which he has no equity other than that of a lessee, user or possessor;

(iv) A reasonable allowance for entertainment, amusement and recreation expenses during the taxable year, that are directly connected to the development, management and operation of the trade, business or profession of the taxpayer, or that are directly related to or in furtherance of the conduct of his or its trade, business or exercise of a profession not to exceed such ceilings as the Secretary of Finance may, by rules and regulations prescribe, upon recommendation of the Commissioner, taking into account the needs as well as the special

circumstances, nature and character of the industry, trade, business, or profession of the taxpayer: Provided, That any expense incurred for entertainment, amusement or recreation that is contrary to law, morals, public policy or public order shall in no case be allowed as a deduction.

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

xxx

xxx

xxx

(B) *Interest.* —

(1) *In General.* — The amount of interest paid or incurred within a taxable year on indebtedness in connection with the taxpayer's profession, trade or business shall be allowed as deduction from gross income: Provided, however, That the taxpayer's otherwise allowable deduction for interest expense shall be reduced by forty-two percent (42%) of the interest income subjected to final tax: Provided, That effective January 1, 2009, the percentage shall be thirty-three percent (33%).

When a taxpayer claims a deduction, it must point to a specific provision of the statute authorizing such deduction and be able to prove entitlement thereto.⁵⁴ The taxpayer must substantially prove by evidence or records the deductions claimed under the law, otherwise, the same will be disallowed.⁵⁵

There are three conditions for the deductibility of a business expense, viz.:

⁵⁴ *Atlas Consolidated Mining and Development Corporation vs. Commissioner of Internal Revenue*, G.R. No. L-26911, January 27, 1981, 55 SCRA 5; *Commissioner of Internal Revenue v. Atlas Consolidated Mining and Development Corporation and Court of Tax Appeals*, G.R. No. L-26924, January 27, 1981, 102 SCRA 246.

⁵⁵ *Id.*

1. the expense must be ordinary and necessary;
2. it must be paid or incurred within the taxable year; and
3. it must be paid or incurred in carrying on a trade or business.

In the case of *H. Tambunting Pawnshop, Inc. v. Commissioner of Internal Revenue*,⁵⁶ the Supreme Court ruled that the requisites for the deductibility of ordinary and necessary trade or business expenses, like those paid for security and janitorial services, management and professional fees, and rental expenses, are that: (a) the expenses must be ordinary and necessary; (b) they must have been paid or incurred during the taxable year; (c) they must have been paid or incurred in carrying on the trade or business of the taxpayer; and (d) they must be supported by receipts, records or other pertinent papers. The proper substantiation requirement for an expense to be allowed is the official receipt or invoice, issued by the service providers concerned.⁵⁷ Moreover, cash vouchers must be validated with official receipts to be given probative value.⁵⁸

The findings⁵⁹ of the ICPA, Dy Go and Company, can be summarized as follows:

Items Disallowed based on the 50% Rule	50%	100% Per Tentative ITR	Per ICPA Report (Allowed)	Exhibit
c1. Purchases	5,026,241.50	10,052,483.00	969,810.00	
c2. Salaries/wages & Benefits - Direct Cost/OE	16,606,693.00	33,213,386.00	33,213,386.00	"MM-11"
c3. Materials/supplies/facilities/rental	35,456,972.00	70,913,944.00	64,139,767.81	"MM-12-8"
c4. Other	4,144,631.00	8,289,262.00	1,097,531.13	"MM-13-7"
c5. Fringe Benefits	1,470,550.00	2,941,100.00	2,941,100.04	"MM-14"
c6. Membership fees	25,416.50	50,833.00	12,500.00	"MM-15-1"
c7. Repairs & Maintenance - supplies	3,735,476.00	7,470,952.00	4,907,853.21	"MM-16-1"
c8. Office Supplies	308,798.50	617,597.00	339,110.94	"MM-17-1"
c9. Interest expense	3,258,409.50	6,516,819.00	3,569,823.58	"MM-18-1"
c10. Insurance	1,583,668.50	3,167,337.00	770,563.64	"MM-19-1"
c11. Representation & Entertainment	1,047,274.50	2,094,549.00	1,968,839.14	"MM-20-1"
c12. Transportation & Travel	1,663,209.50	3,326,419.00	1,054,181.27	"MM-21-3"
c13. Communication, light & water	9,945,158.00	19,890,316.00	5,605,960.15	"MM-22-5"

56 G.R. No. 173373, July 29, 2013, citing *Commissioner of Internal Revenue v. Isabela Cultural Corporation*, G.R. No. 172231, February 12, 2007, 515 SCRA 556.

57 *Id.*

58 *Id.*

59 *Exhibit "MM."*

c14.	Recruitment & training	465,915.50	931,831.00	596,665.33	"MM-23-4"
c15.	Administrative Expenses - others	154,041.00	308,082.00	-	"MM-26"
c16.	Bills processing	919,782.00	1,839,564.00	900,502.05	"MM-24-5"
c17.	Others	6,100,489.00	12,200,978.00	221,215.58	"MM-24-4"

Items Disallowed due to Non-Withholding	BIR Assessment	Allowable Expense	Expense that should be Disallowed	Exhibits
d. Not subjected to withholding tax - Sec. 34k, NIRC				
d1. Commissions	206,450.00	109,928.80	96,521.20	"A" to "L"
d2. Rental	33,705,894.80		1,301,248.00	"MM-12-11," "MM-12-12" and "A" to "L"
d3. Professional fee	14,209,693.30		774,245.35	"MM-28"
e. Creditable Withholding Taxes for 2006	518,179.00	483,618.98	34,560.02	"MM-27"

The individual cost and expense items are discussed below in the order presented in the FLD. The Court found that petitioner's claimed deductions, except for interest expense, were not adequately supported by documentary evidence. Hence, respondent's disallowances applying the 50% rule of approximation provided under *Section 2.4(c) of RMC No. 23-00*⁶⁰ are upheld, as follows:

1. *Purchases – Php5,026,241.50*

Based on the Tentative Annual Income Tax Return ("ITR")⁶¹, petitioner declared Php10,052,483.00 worth of Purchases for the taxable year 2006 but based on the ICPA Report, only Php969,810.00 of the said Purchases should form part of the Cost of Sales.

Upon careful examination of the Schedule of Purchases⁶², only the amount of Php6,600.00 was included in the exhibit folder and supported merely by Accounts Payable Vouchers, which are insufficient proof to substantiate the said expense.

2. *Salaries/wages & benefits-direct cost/operating expenses – Php16,606,693.00*

This item represents Salaries, Wages and Benefits declared in the Tentative ITR of petitioner, broken down as follows:

Schedule 3: Direct Charges – Salaries, Wages and Benefits	₱ 16,606,693
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⁶⁰ As cited in the case of *Mariano Zamora v. Collector of Internal Revenue and Court of Tax Appeals*, G.R. No. L-15290, May 31, 1963.

⁶¹ Exhibit "MM-3."

⁶² Exhibit "MM-10-1."

Schedule D: Salaries and Allowances	16,606,693
Total Salaries, Wages and Benefits	P 33,213,386

According to the ICPA Report, the schedule of salaries and wages (*Exhibit "MM-11"*) provides further breakdown of the above, viz.:

Salaries and wages	P 23,976,252.89
SSS and ECC Contribution	1,255,581.70
PAGIBIG Contributions	108,700.00
Employee insurance benefit expense	4,855,058.60
Employee benefit expense - others	43,591.67
Bonus	2,328,941.42
Overtime expense	645,260.60
Total	P 33,213,386.88

Upon careful scrutiny of the records, no *Exhibit "MM-11"* was found. Consequently, petitioner failed to substantiate its Salaries, Wages and Benefit expense.

3. *Materials/supplies/facilities/rental* – Php33,986,422.00

According to the ICPA Report, this item is composed of site and switch utilities, maintenance, roaming settlement, interconnection and other site related costs which are supported by billing statements, official receipts and vouchers. It further discussed that the BIR's assessment for this account was arrived at, as follows:

Per Tentative ITR		
Direct charges - Materials/supplies/facilities/rental	P 150,195,421.00	
Fringe Benefits	2,941,100.00	P 153,136,521.00
Less: Rentals including Site Switch per FS		82,222,577.00
Balance		70,913,944.00
Disallowance at 50%		P 35,456,972.00

Due to the separate line item for fringe benefits found in the FLD (Item c5 above), the ICPA recommended that the 50% disallowance in the amount of Php70,913,944.00 be reduced by the Php2,941,100.00 attributable to Fringe Benefits, and that petitioner be assessed for Php67,972,844.00 (Php70,913,944.00 less Php2,941,100.00) instead.

Upon further review of the related documents, the ICPA only accounted for Php64,139,767.81 *per Exhibit "MM-12-8."*

While the Court agrees that there was double assessment for Fringe Benefit Expense, it disagrees with the amount of Materials/supplies/facilities/rental found by the ICPA. Upon careful scrutiny of the exhibits, the Court came up with its own findings, to wit:

Items included in the Materials/supplies/facilities/rental account	Per Court's Findings (Allowable Expense)	Exhibit
Site and Switch Utilities	P 21,401,290.50	"MM-12-9"
Site and Switch Maintenance	48,839.55	"MM-12-10"
Rent Expense	1,704,592.78	"MM-12-12"
Total	P 23,154,722.83	

Out of the Php150,195,421.00 declared as Direct charges - Materials/supplies/facilities/rental account in the Tentative ITR, only Php23,154,722.83 was properly supported by VAT invoices, official receipts and other adequate records. Since petitioner failed to provide other adequate records that will overturn the BIR's assessment, the 50% disallowance should be upheld but in the modified amount of Php33,986,422.00, computed as follows:

Per Tentative ITR	
Direct charges - Materials/supplies/facilities/rental	P 150,195,421.00
Less: Rentals including Site Switch <i>per</i> FS	82,222,577.00
Balance	67,972,844.00
Disallowance at 50%	P 33,986,422.00

4. *Direct cost – others – Php4,144,631.00*

Based on the ICPA Report,⁶³ this item is composed of direct commissions, vehicle maintenance & gasoline, software/hardware maintenance, transportation and travel, and demo equipment cost with an aggregate amount of Php8,289,262.00. It was able to obtain a schedule of this item in *Exhibit "MM-13"* and to account for Php1,097.531.13⁶⁴ based on the supplier's invoices, official receipts and payment vouchers examined.

⁶³ *Exhibit "MM."*

⁶⁴ *Exhibit "MM-13-7."*

However, upon careful scrutiny of the submitted exhibits, below is the summary of the Court's findings, showing petitioner's insufficient proof of this expense:

Items included in the Direct Cost - Others account	Per Court's Findings (Allowable Expense)	Exhibit
Transportation and Travel	P 52,893.69	"MM-13-8"
Computer Hardware Rental	7,857.19	"MM-13-10"
Software/Hardware Maintenance	31,016.60	"MM-13-11"
Vehicle Maintenance & Gasoline	234,797.81	"MM-21-5" or "MM-13-9"
Total	P 326,565.28	

5. *Fringe Benefits – Php1,470,550.00*

According to the ICPA, it was able to obtain a schedule (*Exhibit "MM-14"*) which contained monthly accruals of retirement benefit costs amounting to Php245,091.67 and which was subsequently confirmed by Ms. Leticia Bello, Accounting Manager of petitioner. The ICPA further stated that since such items are mere provisions for retirement benefit costs, they should be included as a reconciling item in petitioner's ITR.

However, upon careful review of the exhibits submitted, the Court was unable to find any exhibit folder supporting the alleged *Exhibit "MM-14."* Neither was there any reconciling computation of a retirement benefit cost in the Tentative ITR.

6. *Membership fees – Php25,416.50*

Based on the ICPA Report, this item represents payments to various organizations, but only the aggregate amount of Php12,500.00⁶⁵ was adequately supported by official receipts, payment vouchers and other related records.

Records reveal that only the amount of Php5,803.57, net of VAT, was properly supported by Provisional Receipt No. 7330 while the other attached Official Receipt No. 255717 was disallowed because it was dated November 14, 2005, which is an out-of-period expense. ~

⁶⁵ *Exhibit "MM-15-1."*

7. Repairs and Maintenance- Supplies – Php3,735,476.00

Based on the ICPA Report, this account represents payments for security, janitorial and building maintenance for various offices of the Company. Using the schedule (*Exhibit "MM-16"*) obtained by the ICPA, it was able to inspect and validate the various sales invoices, official receipts, billing statements and payment vouchers; and ascertain that the amount of Php4,907,853.21 (*Exhibit "MM-16-1"*) was adequately substantiated.

Upon careful scrutiny of the attached documents *per* exhibit folder, the Court came up with the following findings:

Date	OR No.	Invoice No/s.	Vendor Name	Amount (Net of VAT)	Reference Nos. (<i>Exhibit "MM-16-1"</i>)
29-May-06	14973		The Orient Square Condominium Assoc., Inc.	P 132,858.75	14
10-Mar-06	151407		Superior Maintenance Services, Inc.	64,925.45	17, 18
02-May-06	5385		Radar Security & Watchman Agency, Inc.	131,420.97	42 to 45, 210
03-Apr-06		1539	SN Iron Works	1,339.29	54
01-Apr-06		6472	Pag-asa Construction Supply	169.64	54
01-Apr-06		6482	Pag-asa Construction Supply	62.50	54
22-Feb-06		6284	Pag-asa Construction Supply	66.96	54
27-Mar-06	3044		Welcome Supermarket Inc	50.89	54
27-Mar-06		22257	Welcome Engineering and Machine Works	312.50	54
23-Mar-06	649		Christian Gas Air Products	392.86	54
24-Mar-06	11741		Infiltrade Enterprises	580.36	54
21-Mar-06		221915	C.J. Lagman Trading	26.79	54
22-Mar-06		221884	C.J. Lagman Trading	1,750.00	54
29-May-06	6218		Radar Security & Watchman Agency, Inc.	135,404.22	56 to 59
07-Jul-06	5858		Radar Security & Watchman Agency, Inc.	166,624.12	60 to 63, 169, 241
14-Aug-06	5875		Radar Security & Watchman Agency, Inc.	149,765.50	84 to 87, 216, 244
01-Sep-06	5880 & 5881		Radar Security & Watchman Agency, Inc.	154,031.79	88 to 91, 179, 180, 217, 245
30-Oct-06	5895		Radar Security & Watchman Agency, Inc.	154,114.09	99 to 102, 218, 246
30-Nov-06	16459		The Orient Square Condominium Assoc., Inc.	159,257.89	121
14-Mar-06	5927		España Tower Condominium Association, Inc.	15,824.05	153 to 155
08-Aug-06	7251		España Tower Condominium Association, Inc.	18,906.75	156 to 159
13-Nov-06	8101		España Tower Condominium Association, Inc.	11,344.05	161
29-May-06	6218		Radar Security & Watchman Agency, Inc.	19,350.43	168, 240
16-May-06	825		Angelique Square Commercial Building	750.00	175
17-Jul-06	853		Angelique Square Commercial Building	1,500.00	187 to 188
Total Allowable Repairs and Maintenance Expense				P 1,320,829.85	

While the following items were disallowed based on the corresponding reasons:

Reason for Disallowance	Documents Attached <i>per</i> Exhibit Folder
No BIR Authority to Print	Invoice #s 2683, 2684, 2685, 2743, 2716, 32, 39, 2760, 2761, 2936, 2924, 2937, 2939, 2938, 2944, 2942, 2936, 2924, 2937, 2939, 2942, 2683, 2684, 2685, 2743, 2716, 32, 39, 2760, 2761, 2924, 2936, 2937, 2939, 2938, 2944, 2942, 2683, 2684, 2685, 2743, 2716, 2760, & 2924

Not in the name of petitioner	Cash Invoice #s 2711, 94430, & 144651; Sales Invoice #7232
Out of Period	Cash Invoice #s 2693, 2321, 2345, 2440, 2355, 202824, 2305, 2924, & 94430; Sales Invoice #33721; Official Receipt #5741
Documents submitted are inadequate to support the declared expense amount	SOA #s 137274, 37272, 138942, 138941, 138437, 140963, 140968, 141213, 142449, 142450, 142451, 145019, 145018, 144655, 144281, 144280, 142519, 143505, 145748, 145849, 146472, 146471, 148027, 148030, 147505, 147510, 149078, 150668, 149068, & 150687; PO #3084
Included in the ICPA Schedule but the document cannot be found in Exhibit "MM-16-1"	OR #s 5889 & 5385

8. Office Supplies – Php308,798.50

Based on the ICPA Report, this item represents disbursements for printing of customized checks, official receipts, copy paper, toners and other supplies which were disbursed through petty cash fund or payment vouchers. Upon examination of sales invoices, official receipts and payment vouchers of the schedule (*Exhibit "MM-17"*), the ICPA noted that the amount of Php339,110.94 was found to be in order.

Upon careful review of the documents in the said exhibit folder, the Court found the following:

Date	OR No.	Invoice No/s.	Vendor Name	Amount (Net of VAT)	Reference Nos. (<i>Exhibit "MM-17-1"</i>)
14-Feb-06		17341	Hans Paper Corporation	₱ 4,892.86	2, 5, 6, 7, 27, 28, 52, 53, 68, 98, 118
24-Feb-06	1153		Arts and Colours	267.86	8
27-Jul-06		A-114144	TCA The Computer Authority Inc.	2,633.93	11
28-Mar-06		24351	Advance Computer Forms, Inc.	20,432.08	13
21-Jul-06	98792		Consolidated Paper Products, Inc.	29,079.24	16
18-Aug-06		204667	Consolidated Paper Products, Inc.	16,785.71	20
25-Oct-06		4942A	Global Computer Forms Corp.	13,500.00	21
24-Oct-06		4943A	Global Computer Forms Corp.	5,785.71	21
16-Jan-06	1		Gepcom Trading & Services	1,732.14	23
16-Jan-06	2		Gepcom Trading & Services	1,540.18	23
17-Mar-06	34812		Agua Vida Systems, Inc.	6,843.75	24
31-Jan-06	1029		Arts and Colours	267.86	25
02-Feb-06		52921	Agua Vida Systems, Inc.	1,125.00	29
02-Feb-06		52943	Agua Vida Systems, Inc.	312.50	29
09-Feb-06		53024	Agua Vida Systems, Inc.	1,218.75	29
09-Feb-06		53031	Agua Vida Systems, Inc.	312.50	29
16-Feb-06		53109	Agua Vida Systems, Inc.	1,125.00	29
16-Feb-06		53121	Agua Vida Systems, Inc.	312.50	29
23-Feb-06		53206	Agua Vida Systems, Inc.	1,093.75	29
23-Feb-06		53210	Agua Vida Systems, Inc.	312.50	29
22-Feb-06		145	Dela Peña Copy System & General Merchandise	44.64	30
20-Feb-06		1049	Arts and Colours	535.71	30

16-Mar-06	PR 31345 & PR 31344		Car Finder Publishing Corp.	1,071.43	31
04-Apr-06		53694	Agua Vida Systems, Inc.	312.50	34
06-Apr-06		53724	Agua Vida Systems, Inc.	1,187.50	34
11-Apr-06		53774	Agua Vida Systems, Inc.	1,375.00	34
11-Apr-06		53790	Agua Vida Systems, Inc.	312.50	34
20-Apr-06		53870	Agua Vida Systems, Inc.	1,281.25	34
27-Apr-06		53955	Agua Vida Systems, Inc.	1,343.75	34
28-Apr-06		53970	Agua Vida Systems, Inc.	312.50	34
04-May-06		54029	Agua Vida Systems, Inc.	1,343.75	36
11-May-06		54127	Agua Vida Systems, Inc.	1,250.00	36
12-May-06		54144	Agua Vida Systems, Inc.	312.50	36
18-May-06		54211	Agua Vida Systems, Inc.	1,843.75	36
25-May-06		54294	Agua Vida Systems, Inc.	1,281.25	36
04-Jun-06		54389	Agua Vida Systems, Inc.	1,562.50	38
01-Jun-06		54394	Agua Vida Systems, Inc.	312.50	38
08-Jun-06		54482	Agua Vida Systems, Inc.	1,531.25	38
15-Jun-06		54559	Agua Vida Systems, Inc.	1,312.50	38
22-Jun-06		54650	Agua Vida Systems, Inc.	1,343.75	38
22-Jun-06		54660	Agua Vida Systems, Inc.	312.50	38
29-Jun-06	40507	54743	Agua Vida Systems, Inc.	1,406.25	38
06-Jul-06		54825	Agua Vida Systems, Inc.	1,531.25	40
10-Jul-06		54857	Agua Vida Systems, Inc.	312.50	40
13-Jul-06		54908	Agua Vida Systems, Inc.	1,437.50	40
20-Jul-06		54987	Agua Vida Systems, Inc.	1,312.50	40
27-Jul-06		55066	Agua Vida Systems, Inc.	1,312.50	40
28-Jul-06		55034	Agua Vida Systems, Inc.	312.50	40
03-Aug-06		55138	Agua Vida Systems, Inc.	1,250.00	43
10-Aug-06	41904	55217	Agua Vida Systems, Inc.	1,437.50	43
14-Aug-06		55265	Agua Vida Systems, Inc.	312.50	43
17-Aug-06		55301	Agua Vida Systems, Inc.	1,343.75	43
24-Aug-06		55367	Agua Vida Systems, Inc.	1,093.75	43
28-Aug-06		55408	Agua Vida Systems, Inc.	312.50	43
31-Aug-06		55452	Agua Vida Systems, Inc.	1,218.75	43
18-Jan-06		212946	Silicon Valley	1,340.91	48
10-Mar-06		33310	Power Mac Center	6,696.43	54
06-Apr-06		6578	Pag-asa Construction Supply	40.18	58
02-Jun-06	92		Liberty Ventures, Inc.	361.85	71
01-Jun-06		80468	Romeo V. Austria Trading	2,500.00	72
23-Jun-06	1314		Arts and Colours	267.86	73
09-Sep-06		83448	Romeo V. Austria Trading	1,160.71	81
29-Nov-06		85765	Romeo V. Austria Trading	2,321.43	81
02-Jan-06	84		Joca Enterprises	227.27	88
22-Mar-06		17584	Celltron Marketing Co.	954.55	90
30-May-06		60028	Multicom Supply Center, Inc.	1,392.85	91
01-Jun-06		74435	Nextel Oriental	71.43	91
01-Jun-06			Malo Gen. Merchandise (the Invoice No. is not visible)	26.79	91
30-May-06		148709	NEXTEL Kevoltronics Center	26.79	91
31-May-06		1195	NEXTEL Communications Philippines, Inc.	446.43	91
31-May-06		525356	Solid Electronics Center	21.43	91
01-Jun-06		293736	Alexan Commercial	15.18	91
31-May-06		1368	Solar Communications Gen Mdsg Co.	580.36	91
30-May-06		290206	AVESCO	307.14	91
31-May-06		40491	H Electrical & Industrial Supply Corp.	304.46	91
10-Feb-06		51120	Screw City Hardware	20.91	92
10-Feb-06		645	Tee To Suy Hardware - Branch	1,207.86	92
07-Aug-06	84408		RJPC Telecoms - Branch I	7,142.86	95
10-Jul-06	15947		Jesmilyn's Copy Center & Gen. Merchandise	241.07	96
20-Dec-06	85128		RJPC Telecoms - Branch I	3,571.43	97
04-Apr-06	65		Sayoc Internet Café	32.14	105
28-Mar-06	712		ABC Solution Enterprises	1,169.64	106
03-Jan-06		142290	Welcome Supermart Inc.	82.73	116
21-Feb-06		28270	Sureknock Trading	127.27	120
21-Feb-06		28268	Sureknock Trading	122.73	120
08-Mar-06		1752	Celltron Marketing Co.	357.14	120
09-Feb-06	5053		PG Pawnshop Branch - I	316.07	120
14-Jun-06		31971	Purewater	71.43	120
23-Jan-06		32089	Purewater	72.73	120
10-Apr-06		160430	Y2K Screw Hardware	89.29	122
12-Jul-06		2114	Welcome Supermart Inc.	41.29	126
22-Sep-06		3995	Welcome Supermart Inc.	1,030.00	129
19-Oct-06		56814	Japan Parts Trading Center	142.86	130
19-Nov-06	902		ALVA Computer & Photocopy Services	33.48	131
06-Dec-06		40885	Makati MICROSHOP	687.50	131

24-Nov-06	1389		National Telecommunications Communication	1,250.00	131
19-Aug-06		45479	MRV Refrigeration & Air Conditioning Parts & Supplies	383.93	131
27-Oct-06		32065	ROTA-Cool Ref & Air Conditioning Supplies	312.50	138
27-Oct-06		23127	LETACO Industrial Gas Center	312.50	138
19-Jan-06	895		Joca Enterprises	1,272.73	141
19-Jun-06		831	Techfinity, Inc	3,214.29	142
Jan-06	425, 424, 429, and 431		Marlyn Beauty Shop	33.00	144
06-Jan-06		227926	Johnnys Supermarket	114.32	144
02-Feb-06		230640	Johnnys Supermarket	113.39	146
29-Mar-06		71566	Enigma	1,084.82	147
16-May-06		34790	Purewater	142.86	148
09-May-06		34645	Purewater	178.57	148
27-Apr-06		34357	Purewater	142.86	148
11-Feb-06		33986	Purewater	178.57	148
22-Mar-06		33488	Purewater	178.57	148
06-Mar-06		33100	Purewater	178.57	148
08-Jul-06		36634	Purewater	142.86	153
07-Jul-06		36195	Purewater	35.71	153
21-Jun-06		35816	Purewater	142.86	153
01-Jun-06		35169	Purewater	178.57	153
Total Allowable Office Supplies Expense				₱ 189,566.53	

While the following documents were disallowed based on the following:

Reason for Disallowances	Documents Attached <i>per</i> Exhibit Folder
Out of period	SI #s 50882, 51043, 51124, 51210, 51362, 51398, 51584, 51622, 51788, 92731, 36473, 17372, 17479, 31744, 92599 & 92731 ref. no. 154; OR #s 842, 738 (p. 87), 95011; CI #s 95018, 607459, 238523; Delivery Receipt 368; OR#36 and tape receipts p. 123
The documents are not included in the list but are found in the exhibit folder	SI #s 51849, 51849, 51936, 52094, 52178, 52250, 52468, 52673 & 52696
Official Receipt not in compliance with BIR Rules	p. 42; p. 63; Rompa Enterprise Ref. No. 149
	OR # 40507 was included in the ICPA schedule but the amount if still added will be more than the amount being claimed as a deduction
The corresponding documents were not in the name of Next Mobile, Inc.	OR from National Bookstore p. 47; SI # 54930 and Nat'l Bookstore OR (p. 62); p. 70; SI #92599; Nat'l Bookstore OR p.91; SI #83319; OR #226 and Nat'l Bookstore OR (p.96); OR #127; tape receipts for Ref. No. 113; CI #28271; CI #658 (p.125); OR #718 (p.129); OR #900 (p.149)
Document does not refer to Office Supplies and Expense	OR # 37031(Liquidation of medical benefit in the amount of Php308.25)
Documents submitted are inadequate to support the declared expense amount	Petty Cash Voucher 16682 (p.89); Delivery Receipt (DR) No. 424 (p.101); DR#489 and other paper for Ref. No. 102; DR #660 and other docs for Ref. No. 103; DR #560; DR #836; DR #1018; DR#s 892 & 634 (p.113); docs submitted for Ref. No. 114; OR and Tape receipts for Ref. No. 115; Job Order p.129; tape receipts for Ref. No. 138; DR #964 p.143

9. Interest Expense – Php2,652,400.45

Based on the ICPA Report, this item is composed of interest incurred on short-term notes obtained by petitioner mostly from Bank of Commerce, Metropolitan Bank and Trust Company and United Coconut Planters Bank. Upon inspection of the original copies of the official receipts and payment vouchers, the ICPA found that the valid interest expense for 2006 is Php5,118,846.23 and interest expense *per* Tentative ITR included a non-deductible portion in the amount of Php37,525.12, thus the Total Non-Deductible Interest Expense was recomputed based on *Section 34(B)(1) of the 1997 NIRC*⁶⁶, as follows:

Interest income as reported <i>per</i> tentative ITR	₱ 90,970.00
Gross up at 80%	113,712.50
Multiply by non-deductible factor <i>per</i> NIRC	33%
Non-deductible portion of interest expense	₱ 37,525.12

Interest still to be supported by the Petitioner	₱ 1,511,497.15
Non-deductible portion <i>per</i> NIRC	37,525.12
Total Non-deductible	₱ 1,549,022.65

Upon the Court's careful examination of the documents and the Tentative ITR, interest income *per* Tentative ITR is Php545,817.00, instead of Php90,970.00, while the duly supported Interest Expenses are provided below:

Per Bank Official Receipts			Per ICPA Schedule	Allowable Interest Expense	Exhibit "MM-18-1"
Date	OR No.	OR Amount (Non-VAT)			
30-Jan-06	35-000*903	₱ 90,762.00	₱ 90,762.00	₱ 90,762.00	1
19-Jan-06	48-000822	25,522.15	25,522.15	25,522.15	2
07-Feb-06	48-000844	564,827.27	32,113.97	32,113.97	3
08-Feb-09	48-000846	4,501.12	4,501.12	4,501.12	4
09-Feb-06	48-000849	52,742.22	52,742.22	52,742.22	5
14-Feb-06	48-000852	13,824.17	13,824.17	13,824.17	6
16-Mar-06	48-000888	23,179.86	22,645.80	22,645.80	7
No date	48-000877	4,300.92	4,300.92	4,300.92	8
08-Mar-06	48-000875	2,725,538.54	24,413.54	24,413.54	9
15-Mar-06	48-000886	12,198.53	12,198.53	12,198.53	12
31-Mar-06	035-00030**	91,822.50	91,822.50	91,822.50	13
18-Apr-06	4*000918	26,880.13	26,880.13	26,880.13	14
04-Apr-06	035-000-30*5	21,281.88	21,281.88	21,281.88	15
09-May-06	48-000941	128,117.31	5,129.88	5,129.88	17
17-May-06	48-000962	37,465.95	37,465.95	37,465.95	18
18-May-06	48-000963	24,356.63	24,356.63	24,356.63	19
23-May-06	8177-000280	644,369.76	644,369.76	644,369.76	20
30-May-06	35-0003***	292,720.00	132,857.00	132,857.00	21
09-Jun-06	48-000991	7,789.99	7,789.99	7,789.99	22

⁶⁶ "In general. - The amount of interest paid or incurred within a taxable year on indebtedness in connection with the taxpayer's profession, trade or business shall be allowed as deduction from gross income; Provided however, that the taxpayers' otherwise allowable deduction for interest expense shall be reduce by forty-two percent (42%) of the interest income subject to final tax; Provided that effective January 1, 2009, the percentage shall be thirty three percent (33%)"

08-Jun-06	48-000985	3,567.26	3,567.26	3,567.26	23
28-Jun-06	177-00046*0	129,441.66	129,441.66	129,441.66	24
22-Jun-06	3U-000602	27,186.99	27,186.99	27,186.99	25
13-Jul-06	3U-000618	18,695.28	18,695.28	18,695.28	26
11-Jul-06	48-001050	3,908.29	3,908.29	3,908.29	27
21-Jul-06	48-001075	26,869.26	26,869.26	26,869.26	28
31-Jul-06	035-000352	118,513.33	118,513.33	118,513.33	29
08-Aug-06	3U-000652	11,069.63	11,069.63	11,069.63	30
15-Aug-06	48-001102	20,580.98	20,580.98	20,580.98	31
22-Aug-06	48-001108	29,299.22	29,299.22	29,299.22	34
24-Aug-06	8177-000394	730,958.90	730,958.90	730,958.90	35
25-Sep-06	035-000**35	110,283.33	110,283.33	110,283.33	37
05-Oct-06	035-00036**	65,677.08	65,677.08	65,677.08	39
10-Oct-06	48-001202	6,169.01	6,169.01	6,169.01	40
13-Oct-06	48-001221	96,434.70	96,434.70	96,434.70	41
27-Oct-06	035-00**770	20,208.33	20,208.33	20,208.33	42
30-Oct-06	035-00037**	30,312.50	30,312.50	30,312.50	43
03-Nov-06	035-000798	15,812.50	15,812.50	15,812.50	45
23-Nov-06	035-0003*11	110,283.33	110,283.33	110,283.33	46 & 47
23-Nov-06	8177-000450	705,753.43	705,753.43	705,753.43	51
20-Nov-06	035-000**09	8,050.00	8,050.00	8,050.00	52
29-Nov-06	035-000*824	30,312.50	30,312.50	30,312.50	53
28-Nov-06	035-000**22	7,578.13	7,578.13	7,578.13	54
27-Nov-06	035-005**16	20,208.31	20,208.31	20,208.31	55
04-Dec-06	035-0003*31	65,677.08	65,677.08	65,677.08	56
13-Dec-06	1311	98,610.27	98,610.27	98,610.27	57
03-Dec-06	035-00***46	9,479.17	9,479.17	9,479.17	58
11-Dec-06	035-000**41	14,677.08	14,677.08	14,677.08	59
19-Dec-06	1320	2,005,764.01	20,950.81	20,950.81	60
11-Dec-06	1304	82,500.00	82,500.00	82,500.00	61
27-Dec-06	035-00039**2	130,491.66	130,491.66	130,491.66	62
Total		P 9,546,574.15	P 4,044,538.16	P 4,044,538.16	

Thus, the non-deductible portion of interest expense shall be computed as follows:

Interest Expense	P 4,044,538.16
Less: Non-Deductible Portion of Interest Expense <i>per</i> NIRC	
Interest Income P 545,817.00	
Multiply by non-deductible	
factor <i>per</i> NIRC 33%	
Non-deductible Interest Expense	180,119.61
Allowable Interest Expense	P 3,864,418.55

Petitioner was able to provide adequate proof relating to the amount of Php3,864,418.55 out of the disallowed Interest Expense in the amount of Php3,258,409.50 (50% of Php6,516,819.00 in the Tentative ITR). Thus, the disallowed Interest Expense shall be recomputed as follows:

Interest Expense <i>per</i> Tentative ITR	P 6,516,819.00
Less: Allowable Interest Expense	3,864,418.55
Disallowed Interest Expense	P 2,652,400.45

10. Insurance Expense – Php1,583,668.50

According to the ICPA Report, insurance expenses incurred by petitioner pertain to premium payments for all-risk insurance from Prudential Guarantee and Assurance, Inc., performance bonds from Trinity Insurance Consultants, Inc. and Philippines First Insurance. It further declared that after examining the official receipts and payment vouchers of petitioner, only the amount of Php770,563.64 was properly substantiated.

Based on record, only one official receipt, OR No. 463995 dated January 18, 2006, from Prudential Guarantee was attached to support this expense amounting to Php1,458,871.09⁶⁷, net of VAT, which is less than the assessment of the BIR.

11. Representation and entertainment – Php1,047,274.50

The ICPA computed for the ceiling amount that petitioner may claim to be allocated between its sales of goods and services based on *Section 5 of RR No. 10-2002*, as follows:

Nature	Sales/Revenues	Percentage	Apportionment
Sale of Service	₱ 184,312,886	87.996437%	₱ 1,843,128.49
Sale of Goods	25,142,056	12.003563%	251,420.51
Totals	₱ 209,454,942	100.00000%	₱ 2,094,549.00

Nature	Sales/Revenues	Percentage	Ceiling
Sale of Service	₱ 184,312,886	1%	₱ 1,843,128.86
Sale of Goods	25,142,056	.05%	125,710.28
Totals	₱ 209,454,942		₱ 1,968,839.14

Nature	Sales/Revenues	Apportionment	Ceiling	Disallowed
Sale of Service	₱ 184,312,886	₱ 1,843,128.49	₱ 1,843,128.86	₱ -
Sale of Goods	25,142,056	251,420.51	125,710.28	125,710.28
Totals	₱ 209,454,942	₱ 2,094,549.00	₱ 1,968,839.14	₱ 125,710.28

However, upon careful review of the documents in *Exhibit “MM-20-1,”* only the amount of Php199,537.59 have complied with substantiation requirements, to wit:

⁶⁷ *Exhibit “MM-19-1.”*

Date	OR No.	Invoice No/s.	Vendor Name	Amount (Net of VAT)	Reference Nos. (Exhibits "MM-20-1")
06-Jan-06	99194		EDSA Shangri-La	₱ 17,987.40	3
02-Jan-06	34713		EDSA Shangri-La	3,100.73	3
10-Feb-06	16076		EDSA Shangri-La	6,254.19	16
06-Feb-06	16530		EDSA Shangri-La	2,273.70	
09-Feb-06	12680		EDSA Shangri-La	13,510.28	
01-Mar-06	118400		EDSA Shangri-La	6,043.24	8
30-Jan-06	12003		EDSA Shangri-La	3,093.31	9
01-Mar-06	118399		EDSA Shangri-La	58,200.91	10
27-Mar-06	PR# 111		Hotel Inter-Continental Manila	5,960.71	12
28-Feb-06	16641		EDSA Shangri-La	888.71	14
09-Mar-06	3511		Atchie's Resto-Bar Corporation	1,125.00	15
10-Mar-06	3514		Atchie's Resto-Bar Corporation	450.00	15
21-Jul-06	121857		EDSA Shangri-La	17,588.89	27
13-Oct-06	3084		Le Soufflé at Rockwell	24,107.14	31
05-Sep-06	136664		Makati Shangri-La	26,785.71	32
25-Jan-06	10372		Max's Restaurant	1,276.54	39
11-Jan-06	438		Red Ribbon	285.71	39
20-Jan-06		470	French Baker	370.54	39
18-Jan-06	7587		Baker Fresh Foods Philippines, Inc.	7,587.00	39
17-Jan-06	10344		Max's Restaurant	862.60	39
14-Jan-06	693		Red Ribbon	477.23	39
12-Jan-06	4625		Luk Foo International Cuisine, Inc.	1,084.82	49
12-Jan-06		6641	Tower Café	223.21	54
Total Properly Substantiated Meal and Entertainment Expense				₱ 199,537.59	

12. *Transportation and Travel – Php1,663,209.50*

According to the ICPA Report, this item includes expenses for gasoline consumed, vehicle maintenance, travel and lodging expenses; and only the amount of Php1,054,181.27⁶⁸ was able to comply with the substantiation requirements.

However, upon the Court's examination of the records, it was revealed that only the amount of Php287,691.50 was properly substantiated:

⁶⁸ Exhibit "MM-21-3."

Items included in Transportation and Travel	Per Court's Findings (Allowable Expense)	Exhibit
Transportation & Travel	P 52,893.69	"MM-13-8"
Vehicle Maintenance & Gasoline	234,797.81	"MM-21-5" or "MM-13-9"
Total	P 287,691.50	

13. *Communication, light and water – Php9,945,158.00*

The ICPA Report provides that this item pertains to expenses for utilities related to Philippine Long Distance Telephone ("PLDT"), Bayantel Communications, Eastern Telecoms, Meralco and Maynilad Waters Services, Inc., among others. It was able to validate that only the amount of Php5,605,960.15⁶⁹ was properly substantiated by adequate supporting documents.

Upon the Court's scrutiny of the exhibit folders pertaining to this item, the allowable expense in the amount of 3,841,562.50 is lower than the BIR assessment at Php9,945,158.00, viz.:

Items included in the Communication, light and water account	Per Court's Findings (Allowable Expense)	Exhibit
Building Utilities	P 2,023,882.53	"MM-22-6"
Leased Lines	1,713,854.29	"MM-22-7"
Telecom-Local	55,454.74	"MM-22-8"
Telecom-Long Distance	48,370.94	"MM-22-9"
Total	P 3,841,562.50	

14. *Recruitment and training – Php465,915.50*

Based on the ICPA's findings, this includes expenses for training, seminars, staff meetings, job postings, forums and other employee related activities. It was able to vouch that only Php596,665.33 was properly substantiated by adequate records.

However, upon careful examination of the exhibit folders, the Court came up with the finding that petitioner was able to substantiate only Php14,741.71 vis-à-vis the assessment of Php465,915.50, to wit:

⁶⁹ Exhibit "MM-2-5."

Items included in the Trainings and Seminar account	Per Court's Findings (Allowable Expense)	Exhibit
Trainings and Seminars	P 535.71	"MM-23-5"
Recruiting	14,205.99	"MM-23-6"
Total	P 14,741.71	

15. *Administrative Expenses – Others – Php154,541.00*

The ICPA found that this item pertains to payments for bank charges on fund transfers, returned checks, payroll, issuance of manager's check and letter of credits; and was able obtain a schedule of this account (*Exhibit "MM-26"*), to arrive at the disallowance in the amount of Php154,541.00.

A careful scrutiny of the records reveal that there was no *Exhibit "MM-26"* provided. However, based on the ITR, the basis for this line item is the amount of Php309,082.00, which should result to a disallowance in the amount of Php154,541.00, in accordance with the 50% Rule, instead of the assessed amount of Php154,041.00.

16. *Bills Processing – Php919,782.00*

The ICPA Report states that this item includes printing and enveloping of petitioner's bills to customers, service fee for bills payment and credit card; and vouches that the amount of Php900,502.05 was properly substantiated by documents.

However, in the course of the Court's independent examination of the records, it only found one valid invoice, Invoice No. 4289,⁷⁰ to support this expense in the amount of Php2,727.00.

17. *Others – Php6,100,489.00*

The findings of the ICPA provides that this item relates to payments for litigation settlement expenses, settlement of roaming fees, association dues, chattel mortgage fees and other related expenses; it was able to validate Php221,215.58 (*Exhibit "MM-25-4"*) as part of this expense.

⁷⁰ *Exhibit "MM-24-6."*

However, upon careful scrutiny of the records submitted, the Court found that petitioner was able substantiate only up to Php62,631.96, viz.:

Items included in the Others account	Per Court's Findings (Allowable Expense)	Exhibit
Other Income/Expense	₱ 62,631.96	"MM-25-5"
BOD Retainer Fee	-	"MM-25-6"
Total	₱ 62,631.96	

In sum, the total disallowed expenses of petitioner for taxable year 2006, based on the 50% Rule are as follows:

Items Disallowed based on the 50% Rule	Disallowances	Exhibit
Purchases	₱ 5,026,241.50	"MM-10-1"
Salaries/wages & Benefits - Direct Cost/OE	16,606,693.00	"MM-11"
Materials/supplies/facilities/rental	33,986,422.00	"MM-12-8"
Direct Cost - others	4,144,631.00	"MM-13-7"
Fringe Benefits	1,470,550.00	"MM-14"
Membership Fees	25,416.50	"MM-15-1"
Repairs & Maintenance - supplies	3,735,476.00	"MM-16-1"
Office Supplies	308,798.50	"MM-17-1"
Interest Expense	2,652,400.45	"MM-18-1"
Insurance	1,583,668.50	"MM-19-1"
Representation & Entertainment	1,047,274.50	"MM-20-1"
Transportation & Travel	1,663,209.50	"MM-21-3"
Communication, Light & Water	9,945,158.00	"MM-22-5"
Recruitment & Training	465,915.50	"MM-23-4"
Administrative Expenses - Others	154,541.00	"MM-26"
Bills Processing	919,782.00	"MM-24-5"
Others	6,100,489.00	"MM-24-4"
Total	₱ 89,836,666.95	

B. Deficiency Income Tax – Disallowance Due to Non-Withholding of Taxes

The pertinent provision is *Section 34(K) of the 1997 NIRC*, viz.:

SECTION 34. *Deductions from Gross Income.* – Except for taxpayers earning compensation income arising from personal services rendered under an employer-employee relationship where no deductions shall be allowed under this Section other than under Subsection (M) hereof, in computing taxable income subject to income tax under

Sections 24(A); 25(A); 26; 27(A), (B) and (C); and 28(A)(1), there shall be allowed the following deductions from gross income:

xxx

xxx

xxx

(K) *Additional Requirements for Deductibility of Certain Payments.* — Any amount paid or payable which is otherwise deductible from, or taken into account in computing gross income or for which depreciation or amortization may be allowed under this Section, shall be allowed as a deduction only if it is shown that the tax required to be deducted and withheld therefrom has been paid to the Bureau of Internal Revenue in accordance with this Section, Sections 58 and 81 of this Code.

Section 2.58.5 of RR No. 2-98, as amended by RR No. 14-02 and RR No. 17-03, provides additional rules regarding the requirement of deductibility in relation to withholding of taxes, to wit:

Section 2.58.5. Requirements for Deductibility. Any income payment which is otherwise deductible under the Code shall be allowed as a deduction from the payor's gross income only if it is shown that the income tax required to be withheld has been paid to the Bureau in accordance with Secs. 57 and 58 of the Code.

A deduction will also be allowed in the following cases where no withholding of tax was made:

- (A) The payee reported the income and pays the tax due thereon and the withholding agent pays the tax, including the interest incident to the failure to withhold the tax, and surcharges, if applicable, at the time of the audit/investigation or reinvestigation/reconsideration;
- (B) The recipient/payee failed to report the income on the due date thereof, but the withholding agent/taxpayer pays the tax, including the interest incident to the failure to withhold that tax and surcharges, if applicable,

at the time of the audit/investigation or reinvestigation/reconsideration;

- (C) The withholding agent erroneously underwithheld the tax but pays the difference between the correct amount and the amount of tax withheld, including the interest, incident to such error, and surcharges, if applicable, at the time of the audit/investigation or reinvestigation/reconsideration. xxx

1. *Commission – Php0.00*

Based on the BIR Assessment this expense item was disallowed due to non-withholding of taxes. However, upon checking the Tentative ITR and the submitted BIR Forms 2307⁷², the Court found the following:

ATC	Income Payments	Tax Withheld
WC 140	₱ 2,673,057.00	₱ 267,305.70
WI 140	82,528.80	8,252.88
Total	₱ 2,755,585.80	₱ 275,558.58

Out of the assessment in the amount of Php206,450.00, petitioner was able to prove that it withheld taxes for its commissions in the amount of Php275,558.58, hence, the attributable BIR assessment shall be denied and petitioner shall be allowed to deduct the said expense.

2. *Rental – Php7,240,828.00*

According to the ICPA Report, the total rent expense subjected to withholding taxes amounted to Php48,516,682.20, which was compared with rentals in the amount of Php80,921,329.00, allegedly based on the Tentative ITR, which is composed of the following:

Site and switch rental	₱ 73,680,501.00
Building rent	7,240,828.00
Difference	₱ 80,921,329.00

⁷² Exhibits “MM-27-1” to “MM-27-4.”

However, upon review of the Tentative ITR, only the amount of Php7,240,828.00⁷³ relating to Building rent was declared as Rental expense for the taxable year 2006, the allocation thereof was found in Note 19 of the Audited Financial Statement⁷⁴, viz.:

	2006	2005
Cost of sales and services	₱ 73,478,070.00	₱ 77,853,988.00
Administrative expense	8,744,507.00	10,049,722.00
Totals	₱ 82,222,577.00	₱ 87,903,710.00

The examination of BIR Forms No. 2307 and their respective alphalists revealed the following:

ATC	Income Payments	Tax Withheld
WC 100	₱ 36,018,456.20	₱ 1,397,922.81
WI 100	20,558,226.00	1,027,911.30
Total	₱ 56,576,682.20	₱ 2,425,834.12

Consequently, out of the Php82,222,577.00 Rent expense *per* AFS, only Php56,576,682.20 have been subjected to 5% Expanded Withholding Tax, pursuant to RR No. 2-98, as amended.

Considering that petitioner only claimed the deduction in the amount of Php7,240,828.00 as Rent expense in its Tentative ITR and the Court cannot determine whether the same was subjected to withholding tax, only the declared amount of Php7,240,828.00 *per* Tentative ITR should be the disallowed and not the full amount of Php33,705,894.80.

3. *Professional Fee – Php12,932,592.37*

The ICPA found that Professional Fees are mainly composed of payments made for consultancy and audit fees, manpower services and messengerial services, with the amount of Php13,435,447.95 pertaining to payments for services rendered by 4th Dimension Multi-Purpose Cooperative ("4th Dimension") and as such is exempt from payment of income tax pursuant to Article 62 of RA No. 6938⁷⁵, as implemented by Section 3.2 of RR No. 20-01.

⁷³ Exhibit "MM-3."

⁷⁴ Exhibit "MM-9."

⁷⁵ "An Act to Ordain a Cooperative Code of the Philippines."

However, upon careful checking of all the submitted evidence, the Court discovered the following:

ATC	Income Payments	Tax Withheld
WC 011	₱ 4,163,917.93	₱ 624,587.69
WI 010	8,133,114.00	813,311.40
WI 011	15,798,408.70	2,369,761.30
Total	₱ 28,095,440.63	₱ 3,807,660.39

Consequently, out of the declared Professional Fees *per* Tentative ITR amounting to Php41,028,033.00 only Php28,095,440.63 were subjected to withholding tax. Thus, the difference of Php12,932,592.37 (Php41,028,033.00 less Php28,095,440.63) should be disallowed as Professional Fees expense due to non-withholding of tax.

4. *Creditable Withholding Taxes - Php54,128.08*

The BIR disallowed creditable withholding taxes claimed by petitioner in the amount of Php518,179.00 due to absence of Creditable Withholding Tax Certificates or BIR Form No. 2307. Upon its own examination of petitioner’s CWT certificates, the ICPA was able to validate that petitioner was able to present CWT certificates amounting to Php483,618.98 and recommended that the disallowance be reduced to Php34,560.02.

An examination of *Exhibits* “MM-27-1” to “MM-27-4” reveal the following findings:

Creditable Withholding Taxes		Exhibit
First Quarter	₱ 113,218.55	“MM-27-1”
Second Quarter	4,965.15	“MM-27-2”
Third Quarter	202,135.50	“MM-27-3”
Fourth Quarter	143,731.72	“MM-27-4”
Total Creditable Withholding Taxes with BIR Form 2307	₱ 464,050.92	

Consequently, only Php464,050.92 out of the declared CWT *per* Tentative ITR amounting to Php518,179.00 may be used as tax credits from creditable tax withheld. The remaining Php54,128.08 (Php518,179.00 less Php464,050.92) shall be disallowed for failure of petitioner to substantiate the same with BIR Form No. 2307.

In sum, the disallowances due to non-withholding of taxes are:

Items Disallowed due to Non-Withholding	Expense that should be Disallowed	Exhibits
Commissions	₱ -	"A" to "L"
Rental	7,240,828.00	"MM-12-11," "MM-12-12" and "A" to "L"
Professional Fee	12,932,592.37	"MM-28"
Creditable Withholding Taxes for 2006	54,128.08	"MM-27"
Total	₱ 20,227,548.45	

Based on the foregoing discussions, petitioner is liable for a total deficiency tax of **Php33,325,336.74**, broken down as follows:

Taxable Income per return			₱	(3,875,794.00)
Add:	50% Disallowances - Sections 6(B) & 34 1997 NIRC; RMC No. 23-2000			
	Purchases	₱	5,026,241.50	
	Salaries/wages & Benefits - Direct Cost/OE		16,606,693.00	
	Materials/supplies/facilities/rental		33,986,422.00	
	Direct Cost - others		4,144,631.00	
	Fringe Benefits		1,470,550.00	
	Membership fees		25,416.50	
	Repairs & Maintenance - supplies		3,735,476.00	
	Office Supplies		308,798.50	
	Interest expense		2,652,400.45	
	Insurance		1,583,668.50	
	Representation & Entertainment		1,047,274.50	
	Transportation & Travel		1,663,209.50	
	Communication, light & water		9,945,158.00	
	Recruitment & training		465,915.50	
	Administrative Expenses - others		154,541.00	
	Bills processing		919,782.00	
	Others		6,100,489.00	
			₱	89,836,666.95
	Not subjected to withholding tax - Sec. 34(k) 1997 NIRC			
	Commissions	₱	-	
	Rental expense		7,240,828.00	
	Professional fee		12,932,592.37	
			₱	20,173,420.37
Taxable income per investigation			₱	106,134,293.32
2006 Corporate Tax Rate at 35%				35%
Tax Due			₱	37,147,002.66
Less: Tax credits / payments per return		₱	3,875,794.00	
	Less: Unsupported BIR 2307		54,128.08	
			₱	(3,821,665.92)
Deficiency Income Tax Due			₱	33,325,336.74

C. *Compromise Penalty*

Respondent imposed compromise penalties in the aggregate amount of Php22,000.00 on the subject deficiency tax assessments, detailed as follows:

Non-filing of alphalist of income payments subject to withholding tax	₱ 1,000.00
Non-filing of alphalist of compensation	1,000.00
Non-filing of Quarterly Summary List of Sales	4,000.00
Non-filing of MAP	12,000.00
Non-filing of SAWT	4,000.00
Total Amount Due & Collectible	₱ 22,000.00

The Court has ruled in the case of *The Abba's Orchard School, Inc. v. Commissioner of Internal Revenue*, CTA Case No. 8377, November 4, 2014⁷⁶ that it has jurisdiction to compel a taxpayer to pay compromise penalty for it implies a mutual agreement between the taxpayer and the BIR with respect to the tax which is so compromised. Absent any proof that petitioner consented to the compromise penalty, the same should not be imposed, otherwise, its imposition is illegal and unauthorized.⁷⁷

Considering that there is no proof that petitioner agreed to the imposition of the compromise penalty, the same is hereby cancelled.

WHEREFORE, in view of the foregoing, the present Petition for Review is hereby **PARTIALLY GRANTED**. Accordingly, petitioner is hereby **ORDERED TO PAY** deficiency Income Tax for the taxable year ended December 31, 2006, in the modified amount of Php41,656,670.93, inclusive of the 25% surcharge imposed under *Section 248(A)(3) of the 1997 NIRC*, computed as follows:

Type of Tax	Basic Deficiency	25% Surcharge	Total
Income Tax	33,325,161.74	8,331,334.19	41,656,670.93

In addition, petitioner is liable to pay:

1. Deficiency interest at the rate of twenty percent (20%) *per annum* pursuant to *Section 249(B) of the 1997 NIRC* on the basic deficiency Income Tax of Php33,325,161.74 computed from April 15, 2007 until full payment thereof; and

⁷⁶ citing *Sarangani Resources Corporation v. Commissioner of Internal Revenue*, CTA Case No. 8105, November 8, 2013.

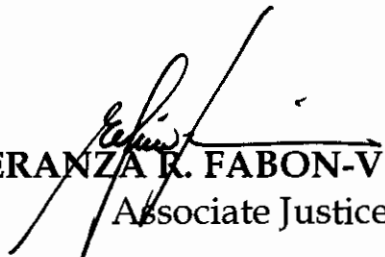
⁷⁷ *Id.*

2. Delinquency interest at the rate of twenty percent (20%) *per annum* on the total amount due of Php41,656,670.93 (inclusive of 25% surcharge), and on the 20% deficiency interest which have accrued as aforestated in (1), computed from May 17, 2010 until full payment thereof, pursuant to *Section 249(C) of the 1997 NIRC*, as amended.

SO ORDERED.


LOVELL R. BAUTISTA
Associate Justice

WE CONCUR:


ESPERANZA R. FABON-VICTORINO
Associate Justice


(With Dissenting Opinion)
MA. BELEN M. RINGPIS-LIBAN
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.


LOVELL R. BAUTISTA
Associate Justice
Chairperson

CERTIFICATION

Pursuant to *Section 13 of Article VIII of the Constitution* and the Division's 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's Division.



ROMAN G. DEL ROSARIO
Presiding Justice

Republic of the Philippines
COURT OF TAX APPEALS
Quezon City

THIRD DIVISION

NEXT MOBILE, INC.,

Petitioner,

CTA CASE NO. 8516

Members:

**Bautista, Chairperson
Fabon-Victorino, and
Ringpis-Liban, JJ.**

-versus-

**COMMISSIONER OF INTERNAL
REVENUE,**

Respondent.

Promulgated:

OCT 14 2015
1:00 p.m.

X-----X

DISSENTING OPINION

With all due respect, I would like to offer my view on the issue of due process raised in this case, namely the validity of a Final Assessment Notice (FAN) issued by the BIR to a taxpayer only ten (10) days after the former issued the latter a Preliminary Assessment Notice (PAN), and without waiting for said taxpayer to respond to the PAN or for the period of fifteen (15) days granted for said response in respondent's own regulations to expire.

The law is clear on the matter. In particular, Section 228 of the National Internal Revenue Code ("Tax Code") provides a clear procedure for protesting of assessments, which is follows:

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 **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 *nd*

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 exciseable 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 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 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 one hundred eighty (180)-day period; otherwise, the decision shall become final, executory and demandable. (Emphasis supplied.)

The word "shall" used above in reference to a taxpayer's response to a preassessment notice or PAN shows that it is mandatory, and the word "required" confirms this. Hence, it is only if the taxpayer fails to respond as required that the Commissioner or his duly authorized representative may issue an assessment based on his findings.

In the instant case, respondent was obligated to wait fifteen (15) days for petitioner to file its response to the former's preassessment notice or PAN, for this is the period that respondent itself provided for in Revenue Regulations No. 12-99, to wit:

"3.1.2 Preliminary Assessment Notice (PAN). — If after review and evaluation by the Assessment Division or 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, at least by registered mail, a Preliminary Assessment Notice (PAN) for the proposed assessment, showing in detail, the facts and the law, rules and regulations, or jurisprudence on which the proposed assessment is based (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." (Emphasis supplied.)

The above administrative provision does not in any way conflict with Section 228 of the Tax Code. Section 228 of the Tax Code itself provides that the period for which to be prescribed by implementing rules and regulations and Revenue Regulations 12-99 are precisely the regulations entitled "Implementing the Provisions of the National Internal Revenue Code of 1997 Governing the Rules on Assessment of National Internal Revenue Taxes."¹ Moreover, taxpayers may rely upon a rule or ruling issued by the Commissioner from the time the rule or ruling is issued up to its reversal by the Commissioner or this Court.²

While the Decision relies on the 2008 case of Commissioner of Internal Revenue vs. Meguito³ where the Supreme Court ruled on the validity of a FAN issued when receipt of the PAN is denied, the same is not on the case here. Here there was manifest violation of due process when respondent disregarded the period that it granted in its own regulations to the detriment of the taxpayer. Such disregard of the authority's own rules and regulations can be very misleading, especially to taxpayers who are not lawyers and follow the BIR's issuances in good faith. They should not be met with bad faith. No good

¹ Complete Title: "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 Taxpayer's Criminal Violation of the Code Through Payment of a Suggested Compromise Penalty"

² Commissioner of Internal Revenue v. San Roque, G.R. No. 187485, October 8, 2013.

³ G.R. No. September 17, 2008.

deed should be punished. More importantly, in 2010 the Supreme Court, in *Revenue vs. Metro Star Superama, Inc.*,⁴ emphasized the importance of complying with the requirement to send a PAN to the taxpayer as an integral part of due process in the issuance of a deficiency tax assessment. It then declared in no uncertain terms that the failure of the CIR to strictly comply with the requirements laid down by law and its own rules is a denial of the taxpayer's right to due process. Undeniably, providing the taxpayer with a copy of the PAN is meaningless to the concept of due process if, after all, his right to respond to it within the prescribed period would be ignored.

Also, in *Pilipinas Shell Petroleum Corporation vs. Commissioner of Internal Revenue*,⁵ the Supreme Court ruled that non-compliance with statutory and procedural due process renders the final assessment notice as null and void even if the taxpayer protested the formal assessment, to wit:

“While PSPC indeed protested the formal assessment, such does not denigrate the fact that it was deprived of statutory and procedural due process to contest the assessment before it was issued. Respondent must be more circumspect in the exercise of his functions, as this Court held in *Roxas v. Court of Tax Appeals*:

“The power of taxation is sometimes called also the power to destroy. Therefore it should be exercised with caution to minimize injury to the proprietary rights of a taxpayer. It must be exercised fairly, equally and uniformly, lest the tax collector kill the ‘hen that lays the golden egg.’ **And in order to maintain the general public’s trust and confidence in the Government this power must be used justly and not treacherously.**”

The above jurisprudence finds application in the instant case where respondent issued a FAN even while the petitioner was still preparing to file its required response to the PAN issued it in accordance with both Section 228 of the Tax Code and Revenue Regulations 12-99, cited above, and disregarding petitioner's rights thereunder. It is clear from Section 228 of the Tax Code that the right to respond to a “preassessment notice” or PAN is given to the taxpayer, and from Revenue Regulations 12-99 that the period of fifteen (15) days to file said response is also the taxpayer's; such rights granted to the taxpayer are not for the taxing authority to waive.

⁴ G.R. No. 185371, December 8, 2010, cited in Hon. Presiding Justice Roman G. Del Rosario's Dissenting Opinion dated August 14, 2015.

⁵ G.R. No. 172598, December 21, 2007, cited in Hon. Presiding Justice Roman G. Del Rosario's Dissenting Opinion dated August 14, 2015.

Moreover, if a statute is clear, plain and free from ambiguity, it must be given its literal meaning and applied without attempted interpretation, hence there is no use debating about the meaning of Section 228 of the Tax Code when its words are very clear.

The FAN issued by the respondent to a petitioner only ten (10) days after the former issued a PAN, and without waiting for said taxpayer to respond to the PAN or for the period of fifteen (15) days granted for said response in respondent's own regulations to expire, is therefore void and of no force and effect.

WHEREFORE, I vote to **GRANT** the Petition.

SO ORDERED.


MA. BELEN M. RINGPIS-LIBAN
Associate Justice