



Republic of the Philippines
Supreme Court
Manila

SECOND DIVISION

COMMISSIONER OF INTERNAL REVENUE, G.R. No. 215957

Petitioner,

Present:

-versus-

CARPIO, *J.*, Chairperson,
BRION,
DEL CASTILLO,
MENDOZA,* and
LEONEN, *JJ.*

FITNESS BY DESIGN, INC.,
Respondent.

Promulgated:
09 NOV 2016

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DECISION

LEONEN, *J.*:

To avail of the extraordinary period of assessment in Section 222(a) of the National Internal Revenue Code, the Commissioner of Internal Revenue should show that the facts upon which the fraud is based is communicated to the taxpayer. The burden of proving that the facts exist in any subsequent proceeding is with the Commissioner. Furthermore, the Final Assessment Notice is not valid if it does not contain a definite due date for payment by the taxpayer.

This resolves a Petition for Review on Certiorari¹ filed by the Commissioner of Internal Revenue, which assails the Decision² dated July

* On official leave.

¹ The Petition was filed under Rule 45 of the Rules of Court.

² *Rollo*, pp. 32–49. The Decision was penned by Associate Justice Juanito Castañeda, Jr. and concurred in by Associate Justices Roman G. Del Rosario, Lovell R. Bautista, Erlinda P. Uy, Caesar A. Casanova, Esperanza R. Fabon-Victorino, Cielito N. Mindaro-Grulla, Amelia R. Cotangco-Manalastas, and Ma. Belen M. Ringpis-Liban.

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14, 2014 and Resolution³ dated December 16, 2014 of the Court of Tax Appeals. The Court of Tax Appeals *En Banc* affirmed the Decision of the First Division, which declared the assessment issued against Fitness by Design, Inc. (Fitness) as invalid.⁴

On April 11, 1996, Fitness filed its Annual Income Tax Return for the taxable year of 1995.⁵ According to Fitness, it was still in its pre-operating stage during the covered period.⁶

On June 9, 2004, Fitness received a copy of the Final Assessment Notice dated March 17, 2004.⁷ The Final Assessment Notice was issued under Letter of Authority No. 00002953.⁸ The Final Assessment Notice assessed that Fitness had a tax deficiency in the amount of ₱10,647,529.69.⁹ It provides:

FINAL ASSESSMENT NOTICE

March 17, 2004

FITNESS BY DESIGN, INC
169 Aguirre St., BF Homes,
Paranaque City

Gentlemen:

Please be informed that after investigation of your Internal revenue Tax Liabilities for the year 1995 pursuant to Letter of Authority No. 000029353 dated May 13, 2002, there has been found due deficiency taxes as shown hereunder:

Assessment No. _____

Income Tax

Taxable Income per return	₱	
Add: Unreported Sales		7,156,336.08
Taxable Income per audit		7,156,336.08
Tax Due (35%)		2,504,717.63
Add: Surcharge (50%)	₱ 1,252,358.81	
<u>Interest (20%/ annum) until 4-15-04</u>	4,508,491.73	5,760,850.54
Deficiency Income Tax		<u>₱ 8,265,568.17</u>

Value Added Tax

³ Id. at 53–57. The Resolution was penned by Associate Justice Juanito Castañeda, Jr. and concurred in by Associate Justices Roman G. Del Rosario, Lovell R. Bautista, Erlinda P. Uy, Caesar A. Casanova, Esperanza R. Fabon-Victorino, Cielito N. Mindaro-Grulla, Amelia R. Cotangco-Manalastas, and Ma. Belen M. Ringpis-Liban.

⁴ Id. at 48, Court of Tax Appeals En Banc Decision.

⁵ Id. at 33.

⁶ Id.

⁷ Id. at 34.

⁸ Id. at 36.

⁹ Id. at 34.

Unreported Sales		₱	7,156,336.08
Output Tax (10%)			715,633.61
Add: Surcharge (50%)	₱	357,816.80	
Interest (20%/ annum) until 4-15-04		<u>1,303,823.60</u>	<u>1,661,640.41</u>
Deficiency VAT		₱	<u>2,377,274.02</u>
Documentary Stamp Tax			
Subscribe Capital Stock		₱	375,000.00
DST due (2/200)			3,750.00
Add: Surcharge (25%)			<u>937.50</u>
Deficiency DST		₱	<u>4,687.50</u>
Total Deficiency Taxes			<u>₱ 10,647,529.69</u>

The complete details covering the aforementioned discrepancies established during the investigation of this case are shown in the accompanying Annex 1 of this Notice. The 50% surcharge and 20% interest have been imposed pursuant to Sections 248 and 249(B) of the [National Internal Revenue Code], as amended. **Please note, however, that the interest and the total amount due will have to be adjusted if paid prior or beyond April 15, 2004.**

In view thereof, you are requested to pay your aforesaid deficiency internal revenue taxes liabilities through the duly authorized agent bank in which you are enrolled within the time shown in the enclosed assessment notice.¹⁰ (Emphasis in the original)

Fitness filed a protest to the Final Assessment Notice on June 25, 2004. According to Fitness, the Commissioner's period to assess had already prescribed. Further, the assessment was without basis since the company was only incorporated on May 30, 1995.¹¹

On February 2, 2005, the Commissioner issued a Warrant of Distrainment and/or Levy with Reference No. OCN WDL-95-05-005 dated February 1, 2005 to Fitness.¹²

Fitness filed before the First Division of the Court of Tax Appeals a Petition for Review (With Motion to Suspend Collection of Income Tax, Value Added Tax, Documentary Stamp Tax and Surcharges and Interests) on March 1, 2005.¹³

On May 17, 2005, the Commissioner of Internal Revenue filed an Answer to Fitness' Petition and raised special and affirmative defenses.¹⁴

¹⁰ Id. at 12-13, Petition for Review. The Annex referred to in the Final Assessment Notice was not attached to the records of the case. However, based on the testimony of Fitness' President, Domingo C. Juan, "[t]he attached details of discrepancy containing the assessment for income tax (IT), value-added tax (VAT) and documentary stamp tax (DST) as well as the Audit Result/Assessment Notices do not impute fraud on the part of petitioner" (Id. at 37, Court of Tax Appeals En Banc Decision).

¹¹ Id.

¹² Id.

¹³ Id.

¹⁴ Id.

The Commissioner posited that the Warrant of Dstraint and/or Levy was issued in accordance with law.¹⁵ The Commissioner claimed that its right to assess had not yet prescribed under Section 222(a)¹⁶ of the National Internal Revenue Code.¹⁷ Because the 1995 Income Tax Return filed by Fitness was false and fraudulent for its alleged intentional failure to reflect its true sales, Fitness' respective taxes may be assessed at any time within 10 years from the discovery of fraud or omission.¹⁸

The Commissioner asserted further that the assessment already became final and executory for Fitness' failure to file a protest within the reglementary period.¹⁹ The Commissioner denied that there was a protest to the Final Assessment Notice filed by Fitness on June 25, 2004.²⁰ According to the Commissioner, the alleged protest was "nowhere to be found in the [Bureau of Internal Revenue] Records nor reflected in the Record Book of the Legal Division as normally done by [its] receiving clerk when she received [sic] any document."²¹ Therefore, the Commissioner had sufficient basis to collect the tax deficiency through the Warrant of Dstraint and/or Levy.²²

The alleged fraudulent return was discovered through a tip from a confidential informant.²³ The revenue officers' investigation revealed that Fitness had been operating business with sales operations amounting to ₱7,156,336.08 in 1995, which it neglected to report in its income tax return.²⁴ Fitness' failure to report its income resulted in deficiencies to its income tax and value-added tax of ₱8,265,568.17 and ₱2,377,274.02 respectively, as well as the documentary stamp tax with regard to capital stock subscription.²⁵

Through the report, the revenue officers recommended the filing of a civil case for collection of taxes and a criminal case for failure to declare Fitness' purported sales in its 1995 Income Tax Return.²⁶ Hence, a criminal complaint against Fitness was filed before the Department of Justice.²⁷

¹⁵ Id.

¹⁶ TAX CODE, sec. 222(a) provides:

Section 222. Exceptions as to Period of Limitation of Assessment and Collection of Taxes.

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

¹⁷ *Rollo*, p. 35, Court of Tax Appeals En Banc Decision.

¹⁸ Id.

¹⁹ Id.

²⁰ Id.

²¹ Id.

²² Id.

²³ Id. at 39.

²⁴ Id. at 35.

²⁵ Id. at 38.

²⁶ Id. at 39.

²⁷ Id.

The Court of Tax Appeals First Division granted Fitness' Petition on the ground that the assessment has already prescribed.²⁸ It cancelled and set aside the Final Assessment Notice dated March 17, 2004 as well as the Warrant of Distrainment and/or Levy issued by the Commissioner.²⁹ It ruled that the Final Assessment Notice is invalid for failure to comply with the requirements of Section 228³⁰ of the National Internal Revenue Code. The dispositive portion of the Decision reads:

WHEREFORE, the Petition for Review dated February 24, 2005 filed by petitioner Fitness by Design, Inc., is hereby **GRANTED**. Accordingly, the Final Assessment Notice dated March 17, 2004, finding petitioner liable for deficiency income tax, documentary stamp tax and value-added tax for taxable year 1995 in the total amount of P10,647,529.69 is hereby **CANCELLED** and **SET ASIDE**. The Warrant of Distrainment and Levy dated February 1, 2005 is likewise **CANCELLED** and **SET ASIDE**.

SO ORDERED.³¹ (Emphasis in the original)

The Commissioner's Motion for Reconsideration and its Supplemental Motion for Reconsideration were denied by the Court of Tax

²⁸ Id. at 67, Petition for Review of the Commissioner of Internal Revenue before the Court of Tax Appeals En Banc.

²⁹ Id. at 40, Court of Tax Appeals En Banc Decision.

³⁰ TAX CODE, sec. 228 provides:

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 pre assessment notice shall not be required in the following cases:

- (a) When the finding for any deficiency tax is the result of mathematical error in the computation of the tax as appearing on the face of the return; or
- (b) When a discrepancy has been determined between the tax withheld and the amount actually remitted by the withholding agent; or
- (c) When a taxpayer who opted to claim a refund or tax credit of excess creditable withholding tax for a taxable period was determined to have carried over and automatically applied the same amount claimed against the estimated tax liabilities for the taxable quarter or quarters of the succeeding taxable year; or
- (d) When the excise tax due on excisable articles has not been paid; or
- (e) When 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.

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.

³¹ *Rollo*, pp. 32–33, Court of Tax Appeals En Banc Decision.

Appeals First Division.³²

Aggrieved, the Commissioner filed an appeal before the Court of Tax Appeals *En Banc*.³³ The Commissioner asserted that it had 10 years to make an assessment due to the fraudulent income tax return filed by Fitness.³⁴ It also claimed that the assessment already attained finality due to Fitness' failure to file its protest within the period provided by law.³⁵

Fitness argued that the Final Assessment Notice issued to it could not be claimed as a valid deficiency assessment that could justify the issuance of a warrant of distraint and/or levy.³⁶ It asserted that it was a mere request for payment as it did not provide the period within which to pay the alleged liabilities.³⁷

The Court of Tax Appeals *En Banc* ruled in favor of Fitness. It affirmed the Decision of the Court of Tax Appeals First Division, thus:

WHEREFORE, the instant Petition for Review is **DENIED** for lack of merit. Accordingly, both the Decision and Resolution in CTA Case No. 7160 dated July 10, 2012 and November 21, 2012 respectively are **AFFIRMED** in toto.³⁸ (Emphasis in the original)

The Commissioner's Motion for Reconsideration was denied by the Court of Tax Appeals *En Banc* in the Resolution³⁹ dated December 16, 2014.

Hence, the Commissioner of Internal Revenue filed before this Court a Petition for Review.

Petitioner Commissioner of Internal Revenue raises the sole issue of whether the Final Assessment Notice issued against respondent Fitness by Design, Inc. is a valid assessment under Section 228 of the National Internal Revenue Code and Revenue Regulations No. 12-99.⁴⁰

³² Id. at 40.

³³ Id.

³⁴ Id. at 41.

³⁵ Id.

³⁶ Id.

³⁷ Id.

³⁸ Id. at 48.

³⁹ Id. at 53-57.

⁴⁰ 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 (1999).

BIR Revenue Reg. No. 12-99, sec. 3.1.4 provides:

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

....

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

Petitioner argues that the Final Assessment Notice issued to respondent is valid since it complies with Section 228 of the National Internal Revenue Code and Revenue Regulations No. 12-99.⁴¹ The law states that the taxpayer shall be informed in writing of the facts, jurisprudence, and law on which the assessment is based.⁴² Nothing in the law provides that due date for payment is a substantive requirement for the validity of a final assessment notice.⁴³

Petitioner further claims that a perusal of the Final Assessment Notice shows that April 15, 2004 is the due date for payment.⁴⁴ The pertinent portion of the assessment reads:

The complete details covering the aforementioned discrepancies established during the investigation of this case are shown in the accompanying Annex 1 of this Notice. The 50% surcharge and 20% interest have been imposed pursuant to Sections 248 and 249(B) of the [National Internal Revenue Code], as amended. Please note, however, that the interest and the total amount due will have to be adjusted *if paid prior or beyond April 15, 2004*.⁴⁵ (Emphasis supplied)

This Court, through the Resolution⁴⁶ dated July 22, 2015, required respondent to comment on the Petition for Review.

In its Comment,⁴⁷ respondent argues that the Final Assessment Notice issued was merely a request and not a demand for payment of tax liabilities.⁴⁸ The Final Assessment Notice cannot be considered as a final deficiency assessment because it deprived respondent of due process when it failed to reflect its fixed tax liabilities.⁴⁹ Moreover, it also gave respondent an indefinite period to pay its tax liabilities.⁵⁰

Respondent points out that an assessment should strictly comply with the law for its validity.⁵¹ Jurisprudence provides that “not all documents coming from the [Bureau of Internal Revenue] containing a computation of

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*” (Emphasis supplied).

⁴¹ *Rollo*, p. 16, Petition for Review.

⁴² *Id.* at 18.

⁴³ *Id.*

⁴⁴ *Id.* at 20.

⁴⁵ *Id.* at 13.

⁴⁶ *Id.* at 87.

⁴⁷ *Id.* at 90–101.

⁴⁸ *Id.* at 91.

⁴⁹ *Id.*

⁵⁰ *Id.*

⁵¹ *Id.*

the tax liability can be deemed assessments[,] which can attain finality.”⁵² Therefore, the Warrant of Distraint and/or Levy cannot be enforced since it is based on an invalid assessment.⁵³

Respondent likewise claims that since the Final Assessment Notice was allegedly based on fraud, it must show the details of the fraudulent acts imputed to it as part of due process.⁵⁴

I

The Petition has no merit.

An assessment “refers to the determination of amounts due from a person obligated to make payments.”⁵⁵ “In the context of national internal revenue collection, it refers to the determination of the taxes due from a taxpayer under the National Internal Revenue Code of 1997.”⁵⁶

The assessment process starts with the filing of tax return and payment of tax by the taxpayer.⁵⁷ The initial assessment evidenced by the

⁵² Id.

⁵³ Id. at 92.

⁵⁴ Id. at 97.

⁵⁵ *SMI-ED Phil. Technology, Inc. v. Commissioner of Internal Revenue*, G.R. No. 175410, November 12, 2014

<<http://sc.judiciary.gov.ph/pdf/web/viewer.html?file=/jurisprudence/2014/november2014/175410.pdf>>
5 [Per J. Leonen, Second Division].

⁵⁶ Id.

⁵⁷ TAX CODE, sec. 56(A) provides:

Section 56. *Payment and Assessment of Income Tax for Individuals and Corporations.*

A) *Payment of Tax.* —

- (1) *In General.* — The total amount of tax imposed by this Title shall be paid by the person subject thereto at the time the return is filed. In the case of tramp vessels, the shipping agents and/or the husbanding agents, and in their absence, the captains thereof are required to file the return herein provided and pay the tax due thereon before their departure. Upon failure of the said agents or captains to file the return and pay the tax, the Bureau of Customs is hereby authorized to hold the vessel and prevent its departure until proof of payment of the tax is presented or a sufficient bond is filed to answer for the tax due.
- (2) *Installment Payment.* — When the tax due is in excess of Two thousand pesos (P2,000), the taxpayer other than a corporation may elect to pay the tax in two (2) equal installments in which case, the first installment shall be paid at the time the return is filed and the second installment, on or before July 15 following the close of the calendar year. If any installment is not paid on or before the date fixed for its payment, the whole amount of the tax unpaid becomes due and payable, together with the delinquency penalties.
- (3) *Payment of Capital Gains Tax.* — The total amount of tax imposed and prescribed under Sections 24(C), 24(D), 27(E)(2), 28(A)(8)(c) and 28(B)(5)(c) shall be paid on the date the return prescribed therefor is filed by the person liable thereto: *Provided*, That if the seller submits proof of his intention to avail himself of the benefit of exemption of capital gains under existing special laws, no such payments shall be required: *Provided, further*, That in case of failure to qualify for exemption under such special laws and implementing rules and regulations, the tax due on the gains realized from the original transaction shall immediately become due and payable, and subject to the penalties prescribed under applicable provisions of this Code: *Provided, finally*, That if the seller, having paid the tax, submits such proof of intent within six (6) months from the registration of the document transferring the real property, he shall be entitled to a refund of such tax upon verification of his compliance with the requirements for such exemption.

tax return is a self-assessment of the taxpayer.⁵⁸ The tax is primarily computed and voluntarily paid by the taxpayer without need of any demand from government.⁵⁹ If tax obligations are properly paid, the Bureau of Internal Revenue may dispense with its own assessment.⁶⁰

After filing a return, the Commissioner or his or her representative may allow the examination of any taxpayer for assessment of proper tax liability.⁶¹ The failure of a taxpayer to file his or her return will not hinder the Commissioner from permitting the taxpayer's examination.⁶² The Commissioner can examine records or other data relevant to his or her inquiry in order to verify the correctness of any return, or to make a return in case of noncompliance, as well as to determine and collect tax liability.⁶³

The indispensability of affording taxpayers sufficient written notice of his or her tax liability is a clear definite requirement.⁶⁴ Section 228 of the National Internal Revenue Code and Revenue Regulations No. 12-99, as amended, transparently outline the procedure in tax assessment.⁶⁵

Section 3 of Revenue Regulations No. 12-99,⁶⁶ the then prevailing regulation regarding the due process requirement in the issuance of a deficiency tax assessment, requires a notice for informal conference.⁶⁷ The revenue officer who audited the taxpayer's records shall state in his or her report whether the taxpayer concurs with his or her findings of liability for deficiency taxes.⁶⁸ If the taxpayer does not agree, based on the revenue

In case the taxpayer elects and is qualified to report the gain by installments under Section 49 of this Code, the tax due from each installment payment shall be paid within thirty (30) days from the receipt of such payments.

No registration of any document transferring real property shall be effected by the Register of Deeds unless the Commissioner or his duly authorized representative has certified that such transfer has been reported, and the tax herein imposed, if any, has been paid.

⁵⁸ *SMI-ED Phil. Technology, Inc. v. Commissioner of Internal Revenue*, G.R. No. 175410, November 12, 2014

<<http://sc.judiciary.gov.ph/pdf/web/viewer.html?file=/jurisprudence/2014/november2014/175410.pdf>> 8 [Per J. Leonen, Second Division]

⁵⁹ *Id.*

⁶⁰ *Id.*

⁶¹ TAX CODE, sec. 6(A).

⁶² TAX CODE, sec. 6(A).

⁶³ TAX CODE, sec. 5(A).

⁶⁴ *Commissioner of Internal Revenue v. Liguigaz Philippines Corp.*, G.R. Nos. 215534 & 215557, April 18, 2016 <sc.judiciary.gov.ph/pdf/web/viewer.html?file=/jurisprudence/2016/april2016/215534.pdf> 7 [Per J. Mendoza, Second Division].

⁶⁵ *Id.*

⁶⁶ On November 28, 2013, Revenue Regulations No. 18-2013 was enacted *amending Certain Sections of Revenue Regulations No. 12-99* relative to the Due Process Requirement in the Issuance of a Deficiency Tax Assessment. The scope of the law provides that under the provisions of Section 244, in relation to Section 245 of the National Internal Revenue Code, as amended, these Regulations are promulgated to amend provisions of Revenue Regulations No. 12-99.

BIR Revenue Reg. No. 18-2013, sec. 2 provides:

Section 2. Amendment. — Section 3 of RR 12-99 is hereby amended by deleting Section 3.1.1 thereof which provides for the preparation of a Notice of Informal Conference, thereby renumbering other provisions thereof, and prescribing other provisions for the assessment of tax liabilities.

⁶⁷ BIR Revenue Reg. No. 12-99, sec. 3.1.1.

⁶⁸ BIR Revenue Reg. No. 12-99, sec. 3.1.1.

officer's report, the taxpayer shall be informed in writing⁶⁹ of the discrepancies in his or her payment of internal revenue taxes for "Informal Conference."⁷⁰ The informal conference gives the taxpayer an opportunity to present his or her side of the case.⁷¹

The taxpayer is given 15 days from receipt of the notice of informal conference to respond.⁷² If the taxpayer fails to respond, he or she will be considered in default.⁷³ The revenue officer⁷⁴ endorses the case with the least possible delay to the Assessment Division of the Revenue Regional Office or the Commissioner or his or her authorized representative.⁷⁵ The Assessment Division of the Revenue Regional Office or the Commissioner or his or her authorized representative is responsible for the "appropriate review and issuance of a deficiency tax assessment, if warranted."⁷⁶

If, after the review conducted, there exists sufficient basis to assess the taxpayer with deficiency taxes, the officer shall issue a preliminary assessment notice showing in detail the facts, jurisprudence, and law on which the assessment is based.⁷⁷ The taxpayer is given 15 days from receipt of the pre-assessment notice to respond.⁷⁸ If the taxpayer fails to respond, he or she will be considered in default, and a formal letter of demand and assessment notice will be issued.⁷⁹

The formal letter of demand and assessment notice shall state the facts, jurisprudence, and law on which the assessment was based; otherwise, these shall be void.⁸⁰ The taxpayer or the authorized representative may administratively protest the formal letter of demand and assessment notice within 30 days from receipt of the notice.⁸¹

II

The word "shall" in Section 228 of the National Internal Revenue Code and Revenue Regulations No. 12-99 means the act of informing the

⁶⁹ BIR Revenue Reg. No. 12-99, sec. 3.1.1 provides that either the Revenue District Office or the Special Investigation Division, as the case may be (in the case of Revenue Regional Offices) or the Chief of Division concerned (in the case of the BIR National Office) may inform the taxpayer of his or her discrepancies.

⁷⁰ BIR Revenue Reg. No. 12-99, sec. 3.1.1.

⁷¹ BIR Revenue Reg. No. 12-99, sec. 3.1.1.

⁷² BIR Revenue Reg. No. 12-99, sec. 3.1.1.

⁷³ BIR Revenue Reg. No. 12-99, sec. 3.1.1.

⁷⁴ Revenue Reg. No. 12-99, sec. 3.1.1 provides that in case of default, 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" shall endorse the case to the Assessment Division.

⁷⁵ BIR Revenue Reg. No. 12-99, sec. 3.1.1.

⁷⁶ BIR Revenue Reg. No. 12-99, sec. 3.1.1.

⁷⁷ BIR Revenue Reg. No. 12-99, sec. 3.1.2.

⁷⁸ BIR Revenue Reg. No. 12-99, sec. 3.1.1.

⁷⁹ BIR Revenue Reg. No. 12-99, sec. 3.1.1.

⁸⁰ BIR Revenue Reg. No. 12-99, sec. 3.1.4.

⁸¹ BIR Revenue Reg. No. 12-99, sec. 3.1.4.

taxpayer of both the legal and factual bases of the assessment is mandatory.⁸² The law requires that the bases be reflected in the formal letter of demand and assessment notice.⁸³ This cannot be presumed.⁸⁴ Otherwise, the express mandate of Section 228 and Revenue Regulations No. 12-99 would be nugatory.⁸⁵ The requirement enables the taxpayer to make an effective protest or appeal of the assessment or decision.⁸⁶

The rationale behind the requirement that taxpayers should be informed of the facts and the law on which the assessments are based conforms with the constitutional mandate that no person shall be deprived of his or her property without due process of law.⁸⁷ Between the power of the State to tax and an individual's right to due process, the scale favors the right of the taxpayer to due process.⁸⁸

The purpose of the written notice requirement is to aid the taxpayer in making a reasonable protest, if necessary.⁸⁹ Merely notifying the taxpayer of his or her tax liabilities without details or particulars is not enough.⁹⁰

*Commissioner of Internal Revenue v. United Salvage and Towage (Phils.), Inc.*⁹¹ held that a final assessment notice that only contained a table of taxes with no other details was insufficient:

In the present case, a mere perusal of the [Final Assessment Notice] for the deficiency EWT for taxable year 1994 *will show that other than a tabulation of the alleged deficiency taxes due, no further detail regarding the assessment was provided by petitioner. Only the resulting interest, surcharge and penalty were anchored with legal basis.* Petitioner should have at least attached a detailed notice of discrepancy or stated an

⁸² *Commissioner of Internal Revenue v. Liquegas Philippines Corp.*, G.R. Nos. 215534 & 215557, April 18, 2016 <<http://sc.judiciary.gov.ph/pdf/web/viewer.html?file=/jurisprudence/2016/april2016/215534.pdf>> [Per J. Mendoza, Second Division]; *Commissioner of Internal Revenue v. Enron Subic Power Corp.*, 596 Phil. 229 (2009) [Per J. Corona, First Division]; *Commissioner of Internal Revenue v. United Salvage and Towage (Phils), Inc.*, 738 Phil. 335 (2014) [Per J. Peralta, Third Division].

⁸³ *Commissioner of Internal Revenue v. Enron Subic Power Corp.*, 596 Phil. 229, 235 (2009) [Per J. Corona, First Division].

⁸⁴ Id.

⁸⁵ Id.

⁸⁶ *Commissioner of Internal Revenue v. Liquegas Philippines Corp.*, G.R. Nos. 215534 & 215557, April 18, 2016 <<http://sc.judiciary.gov.ph/pdf/web/viewer.html?file=/jurisprudence/2016/april2016/215534.pdf>> 14 [Per J. Mendoza, Second Division].

⁸⁷ Id.

⁸⁸ *Commissioner of Internal Revenue v. Metro Star Superama, Inc.*, 652 Phil. 172,187 (2010) [Per J. Mendoza, Second Division].

⁸⁹ *Commissioner of Internal Revenue v. Liquegas Philippines Corp.*, G.R. Nos. 215534 & 215557, April 18, 2016 <<http://sc.judiciary.gov.ph/pdf/web/viewer.html?file=/jurisprudence/2016/april2016/215534.pdf>> 12 [Per J. Mendoza, Second Division].

⁹⁰ Id., citing *Commissioner of Internal Revenue v. Reyes*, 516 Phil. 176, 186–190 (2006) [Per C.J. Panganiban, First Division].

⁹¹ 738 Phil. 335 (2014) [Per J. Peralta, Third Division]

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explanation why the amount of P48,461.76 is collectible against respondent and how the same was arrived at.⁹²

Any deficiency to the mandated content of the assessment or its process will not be tolerated.⁹³ In *Commissioner of Internal Revenue v. Enron*,⁹⁴ an advice of tax deficiency from the Commissioner of Internal Revenue to an employee of Enron, including the preliminary five (5)-day letter, were not considered valid substitutes for the mandatory written notice of the legal and factual basis of the assessment.⁹⁵ The required issuance of deficiency tax assessment notice to the taxpayer is different from the required contents of the notice.⁹⁶ Thus:

*The law requires that the legal and factual bases of the assessment be stated in the formal letter of demand and assessment notice. Thus, such cannot be presumed. Otherwise, the express provisions of Article 228 of the [National Internal Revenue Code] and [Revenue Regulations] No. 12-99 would be rendered nugatory. The alleged "factual bases" in the advice, preliminary letter and "audit working papers" did not suffice. There was no going around the mandate of the law that the legal and factual bases of the assessment be stated in writing in the formal letter of demand accompanying the assessment notice.*⁹⁷ (Emphasis supplied)

However, the mandate of giving the taxpayer a notice of the facts and laws on which the assessments are based should not be mechanically applied.⁹⁸ To emphasize, the purpose of this requirement is to sufficiently inform the taxpayer of the bases for the assessment to enable him or her to make an intelligent protest.⁹⁹

In *Samar-I Electric Cooperative v. Commissioner of Internal Revenue*,¹⁰⁰ substantial compliance with Section 228 of the National Internal Revenue Code is allowed, provided that the taxpayer would be later apprised

⁹² Id. at 349–350.

⁹³ *Commissioner of Internal Revenue v. Liquigaz Philippines Corp.*, G.R. Nos. 215534 & 215557, April 18, 2016 <<http://sc.judiciary.gov.ph/pdf/web/viewer.html?file=/jurisprudence/2016/april2016/215534.pdf>> [Per J. Mendoza, Second Division], citing *Commissioner of Internal Revenue v. United Salvage and Towage (Phils), Inc.*, 738 Phil. 335 (2014) [Per J. Peralta, Third Division], in turn citing *Commissioner of Internal Revenue v. Enron Subic Power Corp.*, 596 Phil. 229 (2009) [Per J. Corona, First Division].

⁹⁴ 596 Phil. 229 (2009) [Per J. Corona, First Division].

⁹⁵ Id. at 235–236.

⁹⁶ Id. at 236.

⁹⁷ Id.

⁹⁸ *Commissioner of Internal Revenue v. Liquigaz Philippines Corp.*, G.R. Nos. 215534 & 215557, April 18, 2016 <<http://sc.judiciary.gov.ph/pdf/web/viewer.html?file=/jurisprudence/2016/april2016/215534.pdf>> 14–15 [Per J. Mendoza, Second Division].

⁹⁹ Id.

¹⁰⁰ G.R. No. 193100, December 10, 2014 <<http://sc.judiciary.gov.ph/pdf/web/viewer.html?file=/jurisprudence/2014/december2014/193100.pdf>> [Per J. Villarama, Jr., Third Division].

in writing of the factual and legal bases of the assessment to enable him or her to prepare for an effective protest.¹⁰¹ Thus:

Although the [Final Assessment Notice] and demand letter issued to petitioner were not accompanied by a written explanation of the legal and factual bases of the deficiency taxes assessed against the petitioner, the records showed that respondent in its letter dated April 10, 2003 responded to petitioner's October 14, 2002 letter-protest, explaining at length the factual and legal bases of the deficiency tax assessments and denying the protest.

Considering the foregoing exchange of correspondence and documents between the parties, we find that the requirement of Section 228 was substantially complied with. Respondent had fully informed petitioner in writing of the factual and legal bases of the deficiency taxes assessment, which enabled the latter to file an "effective" protest, much unlike the taxpayer's situation in *Enron*. Petitioner's right to due process was thus not violated.¹⁰²

A final assessment notice provides for the amount of tax due with a demand for payment.¹⁰³ This is to determine the amount of tax due to a taxpayer.¹⁰⁴ However, due process requires that taxpayers be informed in writing of the facts and law on which the assessment is based in order to aid the taxpayer in making a reasonable protest.¹⁰⁵ To immediately ensue with tax collection without initially substantiating a valid assessment contravenes the principle in administrative investigations "that taxpayers should be able to present their case and adduce supporting evidence."¹⁰⁶

Respondent filed its income tax return in 1995.¹⁰⁷ Almost eight (8) years passed before the disputed final assessment notice was issued. Respondent pleaded prescription as its defense when it filed a protest to the Final Assessment Notice. Petitioner claimed fraud assessment to justify the belated assessment made on respondent.¹⁰⁸ If fraud was indeed present, the period of assessment should be within 10 years.¹⁰⁹ It is incumbent upon petitioner to clearly state the allegations of fraud committed by respondent to serve the purpose of an assessment notice to aid respondent in filing an effective protest.

¹⁰¹ Id. at 12.

¹⁰² Id.

¹⁰³ *Commissioner of Internal Revenue v. Menguito*, 587 Phil. 234, 256 (2008) [Per J. Austria-Martinez, Third Division].

¹⁰⁴ *Tupaz v. Ulep*, 374 Phil. 474, 484 (1999) [Per J. Pardo, First Division].

¹⁰⁵ *Commissioner of Internal Revenue v. Liguiaz Philippines Corp.*, G.R. Nos. 215534 & 215557, April 18, 2016
<<http://sc.judiciary.gov.ph/pdf/web/viewer.html?file=/jurisprudence/2016/april2016/215534.pdf>> 15
[Per J. Mendoza, Second Division],

¹⁰⁶ *Commissioner of Internal Revenue v. Reyes*, 516 Phil. 176, 190 (2006) [Per C.J. Panganiban, First Division]

¹⁰⁷ *Rollo*, p. 33.

¹⁰⁸ Id. at 34.

¹⁰⁹ TAX CODE, sec. 222(a).

III

The prescriptive period in making an assessment depends upon whether a tax return was filed or whether the tax return filed was either false or fraudulent. When a tax return that is neither false nor fraudulent has been filed, the Bureau of Internal Revenue may assess within three (3) years, reckoned from the date of actual filing or from the last day prescribed by law for filing.¹¹⁰ However, in case of a false or fraudulent return with intent to evade tax, Section 222(a) provides:

Section 222. Exceptions as to Period of Limitation of Assessment and Collection of Taxes. —

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

In *Aznar v. Court of Tax Appeals*,¹¹¹ this Court interpreted Section 332¹¹² (now Section 222[a] of the National Internal Revenue Code) by dividing it in three (3) different cases: first, in case of false return; second, in case of a fraudulent return with intent to evade; and third, in case of failure to file a return.¹¹³ Thus:

Our stand that the law should be interpreted to mean a separation of the three different situations of false return, fraudulent return with intent to evade tax and failure to file a return is strengthened immeasurably by the last portion of the provision which aggregates the situations into three different classes, namely “falsity”, “fraud” and “omission.”¹¹⁴

¹¹⁰ TAX CODE, sec. 203 provides:

Section 203. *Period of Limitation Upon Assessment and Collection.* — Except as provided in Section 222, internal revenue taxes shall be *assessed within three (3) years after the last day prescribed by law for the filing of the return*, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period: *Provided,* That in a case where a return is filed beyond the period prescribed by law, the three (3)-year period shall be counted from the day the return was filed. For purposes of this Section, a return filed before the last day prescribed by law for the filing thereof shall be considered as filed on such last day.

¹¹¹ 157 Phil. 510 (1974) [Per J. Esguerra, First Division].

¹¹² TAX CODE, sec. 222(a) provides:

(a) In the case of a false or fraudulent return with intent to evade tax or of a failure to file a return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within ten years after the discovery of the falsity, fraud or omission.

¹¹³ *Aznar v. Court of Tax Appeals*, 157 Phil. 510 (1974) [Per J. Esguerra, First Division].

¹¹⁴ *Id.* at 523.

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This Court held that there is a difference between “false return” and a “fraudulent return.”¹¹⁵ A false return simply involves a “deviation from the truth, whether intentional or not” while a fraudulent return “implies intentional or deceitful entry with intent to evade the taxes due.”¹¹⁶

Fraud is a question of fact that should be alleged and duly proven.¹¹⁷ “The willful neglect to file the required tax return or the fraudulent intent to evade the payment of taxes, considering that the same is accompanied by legal consequences, cannot be presumed.”¹¹⁸ Fraud entails corresponding sanctions under the tax law. Therefore, it is indispensable for the Commissioner of Internal Revenue to include the basis for its allegations of fraud in the assessment notice.

During the proceedings in the Court of Tax Appeals First Division, respondent presented its President, Domingo C. Juan Jr. (Juan, Jr.), as witness.¹¹⁹ Juan, Jr. testified that respondent was in its pre-operating stage in 1995.¹²⁰ During that period, respondent “imported equipment and distributed them for market testing in the Philippines without earning any profit.”¹²¹ He also confirmed that the Final Assessment Notice and its attachments failed to substantiate the Commissioner’s allegations of fraud against respondent, thus:

More than three (3) years from the time petitioner filed its 1995 annual income tax return on April 11, 1996, respondent issued to petitioner a [Final Assessment Notice] dated March 17, 2004 for the year 1995, pursuant to the Letter of Authority No. 00002953 dated May 13, 2002. The attached Details of discrepancy containing the assessment for income tax (IT), value-added tax (VAT) and documentary stamp tax (DST) as well as the Audit Result/Assessment Notice *do not impute fraud on the part of petitioner*. Moreover, it was obtained on information and documents illegally obtained by a [Bureau of Internal Revenue] informant from petitioner’s accountant Elnora Carpio in 1996.¹²² (Emphasis supplied)

Petitioner did not refute respondent’s allegations. For its defense, it presented Socrates Regala (Regala), the Group Supervisor of the team, who examined respondent’s tax liabilities.¹²³ Regala confirmed that the investigation was prompted by a tip from an informant who provided them

¹¹⁵ Id. at 523.

¹¹⁶ Id.

¹¹⁷ *Commissioner of Internal Revenue v. Ayala Securities Corp.*, 162 Phil. 287, 296 (1976) [Per J. Esguerra, First Division].

¹¹⁸ *Commissioner of Internal Revenue v. Air India*, 241 Phil. 689, 698 (1988) [Per J. Gancayco, First Division].

¹¹⁹ *Rollo*, p. 37, Court of Tax Appeals En Banc Decision.

¹²⁰ Id.

¹²¹ Id.

¹²² Id.

¹²³ Id. at 38.

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with respondent's list of sales.¹²⁴ He admitted¹²⁵ that the gathered information did not show that respondent deliberately failed to reflect its true income in 1995.¹²⁶

IV

The issuance of a valid formal assessment is a substantive prerequisite for collection of taxes.¹²⁷ Neither the National Internal Revenue Code nor the revenue regulations provide for a "specific definition or form of an assessment." However, the National Internal Revenue Code defines its explicit functions and effects."¹²⁸ An assessment does not only include a computation of tax liabilities; it also includes a demand for payment within a period prescribed.¹²⁹ Its main purpose is to determine the amount that a taxpayer is liable to pay.¹³⁰

A pre-assessment notice "do[es] not bear the gravity of a formal assessment notice."¹³¹ A pre-assessment notice merely gives a tip regarding the Bureau of Internal Revenue's findings against a taxpayer for an informal conference or a clarificatory meeting.¹³²

A final assessment is a notice "to the effect that the amount therein stated is due as tax and a demand for payment thereof."¹³³ This demand for payment signals the time "when penalties and interests begin to accrue against the taxpayer and enabling the latter to determine his remedies[.]"¹³⁴ Thus, it must be "sent to and received by the taxpayer, and must demand payment of the taxes described therein within a specific period."¹³⁵

The disputed Final Assessment Notice is not a valid assessment.

¹²⁴ Id. at 39.

¹²⁵ Id. Regala admitted that "[i]n their memorandum report, they recommended the filing of a civil case for the collection of petitioner's tax liabilities and a criminal case, for its failure to declare in its ITR for the year 1995 the income derived from its cited sales. Thus, the BIR's filing of a criminal case against petitioner with the Department of Justice (DOJ). The witness confirmed that the gathered information *did not indicate that petitioner's failure to state in its ITR its income and sales for the year 1995 was deliberate*. The instant case was precipitated by the issuance of the Letter of Authority on May 13, 2002." (Emphasis supplied)

¹²⁶ Id.

¹²⁷ *Commissioner of Internal Revenue v. Menguito*, 587 Phil. 234, 256 (2008) [Per J. Austria-Martinez, Third Division].

¹²⁸ *Commissioner of Internal Revenue v. Pascor Realty and Development Corporation*, 368 Phil. 714, 722 (1999) [Per J. Panganiban, Third Division].

¹²⁹ *Tupaz v. Ulep*, 374 Phil. 474, 484 (1999) [Per J. Pardo, First Division]; *Commissioner of Internal Revenue v. Menguito*, 587 Phil. 234, 256 (2008) [Per J. Austria-Martinez, Third Division].

¹³⁰ *Tupaz v. Ulep*, 374 Phil. 474, 484 (1999) [Per J. Pardo, First Division].

¹³¹ *Commissioner of Internal Revenue v. Menguito*, 587 Phil. 234, 256 (2008) [Per J. Austria-Martinez, Third Division].

¹³² Id.

¹³³ Id.

¹³⁴ Id.

¹³⁵ *Commissioner of Internal Revenue v. Pascor Realty and Development Corporation*, 368 Phil. 714, 722 (1999) [Per J. Panganiban, Third Division].

First, it lacks the definite amount of tax liability for which respondent is accountable. It does not purport to be a demand for payment of tax due, which a final assessment notice should supposedly be. An assessment, in the context of the National Internal Revenue Code, is a “written notice and demand made by the [Bureau of Internal Revenue] on the taxpayer for the settlement of a due tax liability that is there definitely set and fixed.”¹³⁶ Although the disputed notice provides for the computations of respondent’s tax liability, the amount remains indefinite. It only provides that the tax due is still subject to modification, depending on the date of payment. Thus:

The complete details covering the aforementioned discrepancies established during the investigation of this case are shown in the accompanying Annex 1 of this Notice. The 50% surcharge and 20% interest have been imposed pursuant to Sections 248 and 249 (B) of the [National Internal Revenue Code], as amended. Please note, *however, that the interest and the total amount due will have to be adjusted if prior or beyond April 15, 2004.*¹³⁷ (Emphasis Supplied)

Second, there are no due dates in the Final Assessment Notice. This negates petitioner’s demand for payment.¹³⁸ Petitioner’s contention that April 15, 2004 should be regarded as the actual due date cannot be accepted. The last paragraph of the Final Assessment Notice states that the due dates for payment were supposedly reflected in the attached assessment:

In view thereof, you are *requested to pay* your aforesaid deficiency internal revenue tax liabilities through the duly authorized agent bank in which you are enrolled *within the time shown in the enclosed assessment notice.*¹³⁹ (Emphasis in the original)

However, based on the findings of the Court of Tax Appeals First Division, the enclosed assessment pertained to remained unaccomplished.¹⁴⁰

Contrary to petitioner’s view, April 15, 2004 was the reckoning date of accrual of penalties and surcharges and not the due date for payment of tax liabilities. The total amount depended upon when respondent decides to pay. The notice, therefore, did not contain a definite and actual demand to pay.

Compliance with Section 228 of the National Internal Revenue Code is a substantive requirement.¹⁴¹ It is not a mere formality.¹⁴² Providing the

¹³⁶ *Adamson v. Court of Appeals*, 606 Phil. 27, 44 (2009) [Per C.J. Puno, First Division].

¹³⁷ *Rollo*, p. 13, Petition for Review.

¹³⁸ *Id.* at 45, Court of Tax Appeals En Banc Decision.

¹³⁹ *Id.*

¹⁴⁰ *Id.* at 46.

¹⁴¹ *Commissioner of Internal Revenue v. BASF Coating + Inks Phils., Inc.*, G.R. No. 198677, November 26,

taxpayer with the factual and legal bases for the assessment is crucial before proceeding with tax collection. Tax collection should be premised on a valid assessment, which would allow the taxpayer to present his or her case and produce evidence for substantiation.¹⁴³

The Court of Tax Appeals did not err in cancelling the Final Assessment Notice as well as the Audit Result/Assessment Notice issued by petitioner to respondent for the year 1995 covering the “alleged deficiency income tax, value-added tax and documentary stamp tax amounting to ₱10,647,529.69, inclusive of surcharges and interest”¹⁴⁴ for lack of due process. Thus, the Warrant of Distraint and/or Levy is void since an invalid assessment bears no valid effect.¹⁴⁵

Taxes are the lifeblood of government and should be collected without hindrance.¹⁴⁶ However, the collection of taxes should be exercised “reasonably and in accordance with the prescribed procedure.”¹⁴⁷

The essential nature of taxes for the existence of the State grants government with vast remedies to ensure its collection. However, taxpayers are guaranteed their fundamental right to due process of law, as articulated in various ways in the process of tax assessment. After all, the State’s purpose is to ensure the well-being of its citizens, not simply to deprive them of their fundamental rights.

WHEREFORE, the Petition is **DENIED**. The Decision of the Court of Tax Appeals En Banc dated July 14, 2014 and Resolution dated December 16, 2014 in CTA EB Case No. 970 (CTA Case No. 7160) are hereby **AFFIRMED**.

SO ORDERED.


MARVIC M.V.F. LEONEN
Associate Justice

<<http://sc.judiciary.gov.ph/pdf/web/viewer.html?file=/jurisprudence/2014/november2014/198677.pdf>>
9 [Per Justice Peralta, Third Division]

¹⁴² Id.

¹⁴³ Id.

¹⁴⁴ *Rollo*, p. 47, Court of Tax Appeals En Banc Decision.

¹⁴⁵ *Commissioner of Internal Revenue v. BASF Coating + Inks Phils., Inc.*, G.R. No. 198677, November 26, 2014
<<http://sc.judiciary.gov.ph/pdf/web/viewer.html?file=/jurisprudence/2014/november2014/198677.pdf>>
9 [Per Justice Peralta, Third Division]

¹⁴⁶ Id. at 9–10, Petition for Review, citing *Commissioner of Internal Revenue v. Algue, Inc.* 241 Phil. 829 (1988) [Per J. Cruz, First Division].

¹⁴⁷ Id.

WE CONCUR:



ANTONIO T. CARPIO

Associate Justice

Chairperson



ARTURO D. BRION

Associate Justice



MARIANO C. DEL CASTILLO

Associate Justice

On official leave

JOSE CATRAL MENDOZA

Associate Justice

ATTESTATION

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



ANTONIO T. CARPIO

Associate Justice

Chairperson, Second Division

CERTIFICATION

Pursuant to Section 13, Article VIII of the Constitution and the Division Chairperson's Attestation, I certify that the conclusions in the above Decision had been reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.



MARIA LOURDES P. A. SERENO

Chief Justice