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## RIGHTS AND REMEDIES OF BOTH THE TAXPAYER AND THE GOVERNMENT IN TAXATION

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### INTRODUCTION

The National International Revenue Code, or the "Tax Code" for short has been substantially revised at least three times during the Marcos Administration and once during the Aquino Administration. We call these periods "BE" and "AE" (Before EDSA and After EDSA).

In view of these major revisions affecting almost all of the provisions of the Tax Code, there is a need for us to revisit and review the provisions especially those that pertain to the rights and remedies of the taxpayer.

Prior to the law that created the Court of Tax Appeals in the 50s, a taxpayer had no remedy against the assessment of the Commissioner of Internal Revenue unless he first paid the tax. This was the case even if the assessment was very clearly illegal, arbitrary or whimsical. Injunction by the courts to prevent collection of the tax was expressly prohibited under the Tax Code.

As they say, "taxes are the life blood of the nation — and the essential functions of government could not afford the resultant delay." This is the reason for not allowing an injunction to prevent the collection of taxes.

With the introduction of different kinds of taxes, it was felt that something had to be done to prevent taxation from being used as an "instrument of oppression." This was when the Board of Tax Appeals, a quasi-judicial body where the taxpayer may litigate and contest an assessment before payment of the tax, was created. To give the Board more stature and to avoid certain legal technicalities, the Board was abolished and elevated to the status of a judicial body, now called the Court of Tax Appeals under Republic Act 1125.<sup>1</sup>

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<sup>1</sup> Amended by RA 3457. [Editors Note: Section 7 of RA 1125 provides for the jurisdiction of the court of Tax Appeals, viz:

The Court of Tax Appeals shall exercise 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 imposed in relation thereto, or other matters arising under

At present therefore, a taxpayer is afforded the opportunity to contest and litigate a tax liability before actually paying the same. This distinguishes the Philippines from some countries, i.e., Indonesia, where a taxpayer must pay first the tax assessed before he can contest the assessment.

A good taxpayer and an ideal corporate officer should always be wary, alert and resourceful in protecting his interest and that of his company on tax matters. If taxes must be paid, it must be to the government and not to anybody else, and the amount paid must only be what is legally due the government, not a centavo more. To be effective in this respect, the taxpayer and/or the corporate officer should be knowledgeable and well-informed about the taxpayer's and the government's rights and remedies in taxation, such as: When is there a valid authority to examine or investigate? When does the government's right to assess and collect a tax prescribe? When should a taxpayer execute or not execute a waiver of the statute of limitations? How should he handle a proposed assessment as distinguished from a formal assessment? When, how, and in what office should he contest a formal assessment? When, how, and where should he file a claim for refund or tax credit? What tax issues or questions should be clarified by a ruling and in what office and in what manner should he file his request for ruling? How can he repel or hold in abeyance the issuance or execution of a distraint or levy proceeding? When and how may he compromise a tax liability?, and such other remedial procedures and administrative matters involving taxation.

It is the intention of this subject or topic to give you a brief, basic and substantive working knowledge of the matter.

### **TAXPAYER'S REMEDIES**

The remedies of a taxpayer may be classified generally into two broad categories:

1. The remedies before payment; and

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the National Internal Revenue Code or other law or part of law administered by the Bureau of Internal Revenue;

(2) Decisions of the Commissioner of Customs in cases involving liability for customs duties, fees or other money charges; seizure, detention or release of property affected; fines, forfeitures or other penalties imposed in relation thereto or other matters arising under the Customs Law or other law or part of law administered by the Bureau of Customs; and

(3) Decisions of provincial or city Boards of Assessment Appeals in cases involving the assessment and taxation of real property or other matters arising under the Assessment Law, including rules and regulations relative thereto.]

2. The remedies after payment.

Before we go into a discussion of these remedies, the validity of a letter of authority (LA) to investigate or examine a taxpayer, should be discussed.

### LETTER OF AUTHORITY TO EXAMINE

Generally, the taxpayer's first encounter with the BIR after filing his return or returns, whether on income, business, *ad valorem* or other types of internal revenue taxes, is when he is served an LA by an examiner or investigating officer of that office. This LA authorizes or empowers the particular examiner or agent to go over, verify and scrutinize his books and records, or, as most of the taxpaying public has experienced, to find fault and errors in the said records no matter how perfect and correct they thought they had prepared and kept the said records. In view of this, to avoid harassment and extortion, the taxpayer should not just open his books and records to anyone who claims to be a BIR examiner and who presents to him an alleged LA without first scrutinizing and checking on the validity of the LA. To be able to do this, the taxpayer must be familiar with what a Letter of Authority is and when it is valid or null and void.

Letters of Authority under applicable Revenue Memorandum Orders (RMO) of the CIR, the latest of which is RMO 28-83 dated September 9, 1983, as amended by RMO 10-89, and RMO 12-89, dated January 31, and February 20, 1989, respectively, shall be issued only by the Commissioner or the Deputy Commissioners or by other officials of the investigating divisions in the National Office who are specifically authorized by the CIR, and by the Regional Directors in the Regional Offices.

It must be pointed out that only one Letter of Authority should be issued for the verification of the income and business tax liabilities of a particular taxpayer or business. This Letter will be issued only to one examiner. It is only when the complexity of the tax case demands it, that more than one examiner may be authorized to examine a taxpayer. These are in very exceptional cases which shall be discussed subsequently.

There have been cases however, arising from situations of conflict of audit jurisdiction, where more than one Letter of Authority has been issued to examine the same taxpayer, for the same taxable year, and for the said internal revenue tax liability. In order to monitor these simultaneous examinations pending the issuance of a Revenue Memorandum Order prescribing guidelines delineating the jurisdiction of the various investigation units, Revenue Memorandum Order 43-88, dated September 16, 1988, provided for a joint examination to be conducted by the Revenue Enforcement Officers designated in the said Letters of Authority. This audit work would be supervised by the immediate superiors and the findings consolidated into one report.

Previously, the Letter of Authority had to specify the years to be examined, with the exception that in cases where unverified years cannot be determined from the records, the Letter may use the phrase, "and all uninvestigated prior years." RMO 10-89 modified this rule by prohibiting the issuance of LAs covering such "unverified prior years," consequently limiting the coverage of each LA to not more than one year.

The name of the Division Chief (National Office) or the Revenue District Officer (Regional Office) should be clearly indicated in the Letter.

As mandated by RMO 12-89, effective February 20, 1989, Letters of Authority may only be issued by the various audit units to investigate internal revenue tax liabilities for calendar year 1987, or fiscal year ended as of June 30, 1987; and prior years. However, the audit and investigation of tax liabilities for calendar year 1988 and all fiscal years beginning after July 1, 1987 remains suspended until further order. In addition, all office audit cases shall be treated as correspondence cases; therefore no LAs shall be issued for such cases.

At present, whenever an LA may be properly issued, RMO 10-89, taken in conjunction with RMO 12-89, prescribe additional requirements for such an issuance. First, the duplicate of the tax returns should be attached to the Letter of Authority. However, the exceptions to this prescription are when "the subject of the investigation has not filed a return or no return is on file at the Assessment Branch as the same may not be located; or where the taxable period is being terminated at any time under Section 16(d) of the National Internal Revenue Code, as amended" (RMO 12-89). These exceptions should be attested by the Chief of the Assessment Branch. Second, no additional Letters of Authority shall be assigned to a revenue enforcement officer who has in his possession twenty or more pending cases for original investigation (see RMO 33-84). If his pending cases are less than twenty, he may be assigned additional cases to replenish those that have been terminated. In no case shall each examiner have more than twenty cases. Third, that the income tax liability of the taxpayer has not been investigated by the same revenue officer for the taxable period immediately preceding the period presently under investigation. Lastly, as already pointed out, the LAs should now cover only one taxable year.

It is very important to remember that the LA must be served to the taxpayer within thirty days from its date of issue; otherwise, it becomes null and void and the taxpayer has all the rights to refuse its service if served beyond the thirty day period. To be able to conduct an examination, the examiner has to have his Letter revalidated or changed by a new one. Any erasures in the LA also gives the taxpayer the right to refuse its service and to consider it null and void.

As distinguished from the thirty day period within which the Letter must be served, an examiner is given only one hundred twenty days from the

date of issuance of the Letter within which to conduct his examination and submit his report of investigation. If the final report cannot be completed within the one hundred twenty day period, a progress report must be submitted by the examiner and the Letter returned for revalidation. The patent implication is that if the one hundred twenty days expire without any report, whether final or progressive, having been submitted by the examiner, the Letter becomes invalid. Under the circumstances, if the examiner returns to continue his examination, he may be refused by the taxpayer unless he presents a revalidated authority. It is, therefore, important for the taxpayer to know who has the jurisdiction to examine a particular taxpayer because this is one of the determinants of the validity of a Letter of Authority.

The Commissioner of Internal Revenue issued Revenue Memorandum Order No. 38-88, dated August 4, 1988, indicating certain guidelines on the revalidation of Letters of Authority. The guidelines limited the revalidation of the Letters to only once in the Regional Offices and twice in the National Office, after the issuance of the original Letter. The necessary inference drawn from these guidelines is that if the Letter of Authority has already been revalidated once or twice, as the case may be, the Letter may no longer be revalidated in favor of the same examiner or agent. Additionally, under the issued guidelines, revalidation shall be accomplished by issuing a new Letter and attaching the superseded Letters to the new Letter issued. This is unlike the procedure of revalidation resorted to prior to the issuance of RMO 38-88, wherein a simple letter from the Division Head or the BIR Officer concerned certified that the Letter of Authority is validly existing and proper. Currently, a new Letter in its appropriate form will have to be issued to revalidate the one that had lapsed. The guidelines, for enforcement purposes, also require the strict monitoring of the Letters issued to ensure that the required reports are rendered within the reglementary one hundred twenty day period.

### JURISDICTION TO EXAMINE

In connection with the examination of the respective income tax returns and accounting records by the BIR, it is very important to know the internal procedures and policies of the BIR on the matter as well as the groups or divisions that are authorized or involved in the examination. Of course the taxpayer would want to be sure that the examiner who will examine his books belongs to the right division or group having jurisdiction over the examination of his respective returns.

There are three (3) classifications of examinations listed under applicable revenue memorandum orders of the Commissioner, the most recent of which is RMO No. 31-83 dated September 7, 1983.

These are: (1) National Office examination; (2) Regional Office examination; and (3) Coordinated examination.

## NATIONAL OFFICE EXAMINATION

The National Office examination refers also to the so-called industry examination and is conducted by the different examination divisions of the National Office. Before the BIR Reorganization under the new administration, there were then ten examination divisions.

1. Agriculture and Natural Resources Division
  - Forestry
  - Mining
  - Special Project – Fishing, etc.
2. Real Estate & Transfer Tax Division
  - Real estate development, transfers of property by death or donation, etc.
3. Banks, Financing & Insurance Division
4. Government and Tax-exempt Corporations
  - Rural Banks; NACIDA, etc
5. Investment Incentive Division
  - Automotive, etc.
6. International Operations Division
  - International Carriers
  - Multinational corporations, etc.
7. Manufacturing Division I
  - Food Industry/Chemicals, etc.
8. Manufacturing Division II
  - Basic Metal; textile; wearing apparel; leather industries, etc.
9. Construction, Transportation & Service
  - Industry Division
  - Contractors
  - Public utilities – Special project with COA, etc.
10. Franchise & Miscellaneous Taxes Division
  - Trading businesses/franchise grantees/
  - Educational institutions, etc.

Note that each audit division in the National Office has jurisdiction over taxpayers based on the industry classification of the taxpayer, i.e., taxpayers engaged in mining and forestry are under the Agriculture and Natural Resources Division; banks, financing institutions and insurance companies are under the Bank's Financing and Insurance Division, etc. The BIR National Office prepares and keeps a list of taxpayers under the industry classification which are selected for examination by the different audit divisions of the BIR's National office. It is possible that a particular firm, depend-

ing on the line of industry, would be on this list. The list is amended yearly; the amendment consists of listing additional taxpayers and/or delisting those in the previous year's list. So it is possible that a taxpayer may be in the list of National Office examination in a particular year or will not appear in another year, or back again.

After the reorganization of the different offices in the BIR, most of the industry divisions, as mentioned, were reduced to mere "sections" of the Industry Audit Division. Only the Banks Financing and Insurance Division and the International Operations Division (now called "International Tax Affairs Division") were left as divisions. All the rest, like the Agricultural and Natural Resources Division, Manufacturing Division I and Manufacturing Division II, etc., are now mere sections of the so-called "Industry Audit Division."

### REGIONAL OFFICE EXAMINATION

Those not in the list for National Office examination fall under the jurisdiction of the different Regional Offices and are to be examined by Regional Officers, depending on the location or principal place of business.

A bank, therefore, whose office or place of business is in Makati, which is not listed for examination by the National Office, falls under the jurisdiction of the Regional Office in Makati. In other words, even if one is a banking institution or engaged in banking or financing, it does not necessarily mean that one will be examined by the Banks, Financing & Insurance Division. Or a manufacturer may not necessarily be examined by the Manufacturing Division (now a section of the Industry Audit Division of the National Office).

If one is on the list, then one belongs to the National Office. If not, then the Regional Office where one's head office is located has the jurisdiction.

This is how the coverage of a National Office examination or Regional Office examination is defined or explained. This examination is called the "primary audit" jurisdiction to investigate the taxpayer.

It is therefore incumbent upon the taxpayer, once he is served a Letter of Authority, to verify or check from the BIR's National Office whether he is listed or not for National Office investigation. If he is listed and the LA being served on him is issued by the Regional Office then such Letter of Authority is not issued by the proper office or jurisdiction within the BIR and he may refuse examination under that particular LA. If he is being served an LA issued by the National Office and he is not listed in its list of taxpayers to be examined, then the jurisdiction to examine him belongs to the Regional Office and he can outright refuse examination by the National Office. This is to avoid duplication of examination by the different groups of examiners as well as harassment of taxpayers.

## COORDINATED EXAMINATION

The third classification is the "Coordinated Examination" of the BIR or the so-called "joint or concurrent examination."

Under this program, another division coordinates with the division having *primary audit* jurisdiction and conducts a joint examination of the taxpayers. Appropriately, we say that his other division has a *functional audit* jurisdiction over a taxpayer, as distinguished from the primary audit jurisdiction of the different audit divisions and the regions we have previously discussed. Under this program, although a particular taxpayer is under the primary audit jurisdiction of a particular region, the nature of the business activities may involve a line of business or industry or certain types of tax incentives or exemption which would or may require the "know-how" of another division in its investigation. This is the case where the so-called "functional audit jurisdiction" of a certain audit division would have to come in, resulting in a so-called "joint or coordinated examination" of the taxpayer.

In accordance with RMO 32-83 of October 18, 1983, the Commissioner of Internal Revenue has nominated the Investment Incentives Division, now a mere section of the Industry Audit Division, and the International Operations Division, now called the International Tax Affairs Division, of the BIR's National Office as functional audit divisions or having so-called "functional audit" jurisdiction over taxpayers whose primary audit are within the jurisdiction of the regions or different divisions of the National Office.

The Industry Audit Division, through its Investment Incentives Section, is the audit division in the National Office that has the expertise in the examination and handling of taxpayers enjoying tax incentives, while the International Tax Affairs Division (formerly IOD) is the division that has developed "know-how" in the handling and examination of multi-national or international companies and overseas workers and contractors.

Under the coordinated examination program, in addition to the division or region having primary audit jurisdiction over a taxpayer, the Investment Incentives Section of the Industry Audit Division or the International Tax Affairs Division, as the case may be, is authorized to conduct a joint or concurrent examination of the taxpayers.

A food manufacturer therefore that is registered as an exporter under the Board of Investments (BOI) enjoying certain tax exemptions under the applicable investment incentives law and that is not listed in the National Office List and therefore under the primary audit jurisdiction of the Region can, under the coordinated examination program, be concurrently or jointly examined by both the Regional examiners where the office of the food ma-



manufacturer is located and the Investment Incentives Section of the Industry Audit Division of the BIR National Office.

The Commissioner's policy is to determine the necessity of a coordinated examination on a case-to-case basis and therefore determine and properly authorize the division that will perform the functional audit jurisdiction.

In cases where a coordinated examination is required, a report of examination shall not be submitted for approval unless it also contains the recommendation and report of the coordinating division.

### OTHER SPECIAL EXAMINATIONS

Aside from the previously mentioned examinations by the Regional Office or by the National Office, or by both, in the case of a coordinated examination, there is what is called the examination by the so-called "Special Investigation Team."

These Special Investigation Teams are groups of examiners especially organized by the Commissioner of Internal Revenue himself and would as a general rule report directly to the Commissioner. The Commissioner would assign his teams or groups specific cases for examination and investigation and they report their findings directly to the Commissioner. The procedure of their investigation would fall under the regular procedure of examination, the legality of their Letters of Authority would also be governed by the requirements of a valid LA and the LAs would normally be signed by the Commissioner himself.

### EXAMINATION ONLY ONCE: PRESERVATION OF BOOKS OF ACCOUNTS

At this point, I would like to make clear that for income tax purposes, a taxpayer may be examined only once, covering a particular taxable year. This is in accordance with Section 235<sup>2</sup> of the Tax Code.

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<sup>2</sup>SEC. 235. Preservation of books of accounts and other accounting records - All books of accounts including the subsidiary books, and other accounting records of corporations, partnerships, or persons shall be preserved by them for a period beginning from the last entry in each book until the last day prescribed by Section 203 within which the Commissioner is authorized to make an assessment. The said books and records shall be subject to examination and inspection by internal revenue officers: Provided, that for income tax purposes, such examination and inspection shall be made only once in a taxable year, except in the following cases;

The taxpayer is also obliged to preserve his books for a period beginning from the last entry in each book until the last day prescribed by Section 203 within which (the Commissioner is authorized to make an assessment, which is three years, unless there is a pending tax examination, in which case the books must be preserved until the case is terminated.

One will note from the provisions of Section 235 that taxpayers are protected from multiple examination of his income tax liability for the same year. Therefore even if one is presented a genuine Letter of Authority, if one has already been examined for the same period, one may refuse the second examination and consider the Second LA invalid. There are of course exceptions to this rule, as follows:

1. When the Commissioner determines that there is fraud, irregularity or mistake committed by the taxpayer;
2. When the taxpayer himself requests a reinvestigation or re-examination;
3. In the case of verification of compliance with the withholding tax requirements;
4. In the case of verification of capital gains tax liabilities; and
5. When the Commissioner exercises his power to obtain information relative to the examination of other taxpayers under Section 7(b) of the Tax Code.

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- (a) Fraud, irregularity or mistakes as determined by the Commissioner;
  - (b) The taxpayer requests reinvestigation;
  - (c) Verification of compliance with withholding tax laws and regulations;
  - (d) Verification of capital gains tax liabilities; and
  - (e) In the exercise of the Commissioner's power under Section 7 (b) to obtain information from other persons, in which case, another or separate examination and inspection may be made. Examination and inspection of books of accounts and other accounting records shall be done in the taxpayer's office or place of business or in the office of the Bureau of Internal Revenue. All corporations, partnerships or persons that retire from business shall, within ten days from the date of retirement or within such period of time as may be allowed by the Commissioner in special cases, submit their books of accounts, including the subsidiary books and other accounting records to the Commissioner or any of his deputies for examination, after which they shall be returned. Corporations and partnerships contemplating dissolution must notify the Commissioner; and shall not be dissolved until cleared of any tax liability.

Any provision of existing general or special law to the contrary notwithstanding, the books of accounts and other pertinent records of tax-exempt organizations or grantees of tax incentives shall be subject to examination by the Bureau of Internal Revenue for purposes of ascertaining compliance with the conditions under which they have been granted tax exemptions or tax incentives, and their tax liability, if any. (As amended by P.D. No. 1959)

In the case of the preservation of a taxpayer's books and records, a taxpayer may no longer be required to produce his records beyond the period of preservation required by law.

(E.G.      - 1980 records   - 5-year Prescriptive Period  
                   Last entry       - Dec. 31, 1980  
                   Filed return   - April 15, 1981  
                   Preserve up to - April 15, 1986) ← 25 yrs? period allowed by 3203 11-1-81 is only 3 yrs

It is therefore advisable to keep books and records separately for each year so that those that should not be kept anymore may be segregated from the current ones.

### LOG BOOK OR BIR REGISTER

In connection with the examination of taxpayers and visits by BIR examiners, another good practice is to keep a log book or register wherein BIR examiners who call on taxpayers are made to register or sign and indicate therein the time and date of their arrival and departure. This is authorized by an old Memorandum of the BIR and would be a good practice which could be a deterrent to any ill-intentioned persons as well as make BIR examiners truly do their examination work properly.

### LETTER OF CONFIRMATION/TERMINATION LETTER

Prior to *RMO 28-83*, after an examination is terminated, a so-called "letter of confirmation" (LC) is issued by the BIR official concerned, usually the Division Head of the National Office or the Regional District Officer of the Regional Office, as the case may be to confirm that the examination has been terminated or a tax liability was found due. For taxpayers who fix or settle their tax cases with examiners, they expect the issuance of the LC to completely close their case. Note, however, that the LC states clearly that the finding stated in the letter either with or without discrepancy is subject to review by higher BIR authorities and therefore, does not terminate or completely close the case.

In view of this misconception and the fact that the letter of confirmation is being used as a tool by unscrupulous BIR personnel, the issuance of letters of confirmation has been completely disauthorized under *RMO 28-83*. In lieu thereof, a more specific and categorical disposition of cases is

effected by means of the so-called "termination letter" which is issued upon approval of the report of the examiner/s. This termination letter is signed by the Commissioner or a Deputy Commissioner, for cases investigated by the National Office, and by the Regional Director or Assistant Regional Director, for cases within the jurisdiction of their regions.

In brief, the termination letter states that the report submitted recommending no discrepancy or an amount of tax liability, has been approved and upon payment of the tax deficiency, if any, the records bearing on the case will be filed for future reference. This is the type of confirmation which, as a general rule, would completely close a tax case for an open year. Normally, the termination letter is issued with the assessment notice if a deficiency is indicated and payment of the deficiency will close the case for all practical purposes. Anything short of the termination letter and the issuance of the deficiency assessment, where applicable, still leaves the case open for further scrutiny, or, very mildly stated, "for review by higher authorities."

#### **POWERS OF THE COMMISSIONER RELATIVE TO INVESTIGATION**

In connection with his power to investigate and examine returns or internal revenue tax liabilities of any person, the Commissioner of Internal Revenue is granted certain powers under Section 7 of the Tax Code.<sup>3</sup>

The more salient feature of this provision is the power given to the Commissioner to enable him to obtain data and information from other parties other than the taxpayer himself. Under Sec. 7, subpar. (3), the Commissioner is empowered to summon any person having possession, custody or care of the books of accounts and other accounting records containing

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<sup>3</sup>SEC. 7. Power of the Commissioner to obtain information, examine, summon and take testimony. — For the purpose of ascertaining the correctness of any return, making a return where none has been made, determining the liability of any person for any internal revenue tax, or collecting any such liability, the Commissioner is authorized:

(1) To examine any book, paper, record or other data which may be relevant or material to such inquiry,

(2) To obtain information from any office or officer of the national and local governments, government agencies or its instrumentalities including the Central Bank of the Philippines and government owned or controlled corporations;

(3) To summon the person liable for tax or required to file a return, or any officer or employee of such person, or any person having possession, custody, or care of the books of accounts and other accounting records containing entries relating to the business of the person liable for tax, or any other person, to appear before the Commissioner or

entries relating to the business of the person liable for tax, or for such other person to appear before the Commissioner, to produce certain books, papers and other data and to give testimony relating to the liability of the person or taxpayer subject to investigation.

This power of the Commissioner to inquire and obtain records from others pertaining to a person under investigation is quite broad. He may obtain these information and records and documents from another private person who has had dealings with the one under investigation. As an example, if a manufacturer or trader is under investigation for any income or business tax liability, the Commissioner, or his duly authorized representative, may go to the suppliers of this manufacturer or trader for information as to the sale of materials, goods or supplies made by them to the manufacturer or trader for purposes of determining their beginning inventories. He may also go to the customers of this manufacturer or trader to determine his gross sales.

Another power of the Commissioner is that contained in Section 16 of the Tax Code. This particularly refers to the authority to conduct inventory taking, surveillance and to prescribe presumptive gross sales and receipts. Under this authority, the Commissioner may at any time during the taxable year place the business operations of a person under observation or surveillance and his findings may be used by him as basis for the other months or quarters of the same or different taxable years and such assessment shall be deemed *prima facie* correct. This authority to conduct surveillance and prescribe presumptive gross sales and receipts was the offshoot of a case wherein the Commissioner issued deficiency assessments against taxpayers by basing the same on surveillance.

In that particular case, the Court said that the Commissioner must base his assessments not on mere presumptions and assumptions but on actual facts. This particular provision cures the adverse effect of the said decision and now deems *prima facie* correct the Commissioner's findings. In this case, the burden is shifted to the taxpayer to prove that the Commissioner's assessment is erroneous.

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his duly authorized representative at a time and place specified in the summons and to produce such books, papers, records, or other data, and to give testimony;

(4) To take such testimony of the person concerned, under oath, as may be relevant or material to such inquiry; and

(5) To cause revenue officers and employees to make a canvass from time to time of any revenue district or region and inquire after and concerning all persons therein who may be liable to pay any internal revenue tax, and all persons owning or having the care, management or possession of any object with respect to which a tax is imposed. (As amended by PD No. 1994)

## GOVERNMENT'S RIGHT TO ASSESS AND/OR COLLECT TAXES

In relation to the government's right to examine or investigate a taxpayer, let us discuss the government's right to assess and/or collect the tax. More specifically, I would like to touch on the periods of limitations within which the government may validity assess and/or collect a tax.

Even if an examiner serves a valid Letter of Authority, the taxpayer need not necessarily open his books and records to the examiner, because if the government's right to assess a taxpayer has already prescribed, then it is futile to examine the taxpayer because the government can no longer validly assess him. If the right of the government to assess has prescribed, it has also lost the right to examine the taxpayer.

Very briefly, the right to assess is the right of the government to examine and determine a taxpayer's tax liability and accordingly notify and demand from him the payment of the said liability. The right to collect is the exercise of the government's remedies to pursue the actual collection of the taxes assessed. As a general rule, before the government can exercise the right to collect, the Commissioner must first validly assess the taxpayer. It is therefore important to know when the government's right to assess the taxpayer prescribes.

Please note that under Section 203<sup>4</sup> and 223<sup>5</sup> of the Tax Code there are two prescriptive periods: the ordinary period and the extraordinary period of prescription.

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<sup>4</sup>SEC. 203. Period of limitation upon assessment and collection. - Except as provided in the succeeding section, internal revenue taxes shall be assessed within three 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-year period shall be counted from the day the return was filed. For the 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 (As amended by B.P. Blg. 700)

<sup>5</sup>SEC. 223. 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 begun without assessment, at any time within ten 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.

Under Section 203, the ordinary period of prescription is three (3) years after the last day prescribed by law for the filing of the return and this is applicable to the taxable year 1984. Before the amendment introduced by B.P. Bldg. 700, its then Section 318 provided for a 5-year period of prescription.

Presently, or beginning the taxable year 1984, it is only within a period of three years from the due date of the filing of the taxpayer's return or the actual date of its filing, if the return was filed after the due date, that the BIR has the power to validly assess the taxpayer. In determining or counting the 3-year period, I would like to emphasize that the due date of the filing of the return, or the actual date of the filing of the return, if the same is actually filed beyond the due date, is the date that should be recognized.

The extraordinary period of prescription to assess and collect a tax under Sec. 223 of the Tax Code is ten (10) years. This period applies where (a) the taxpayer files a false or fraudulent return; or (b) no return was filed.

The 10-year period is counted from the discovery of the falsity, fraud or omission. Unless the taxpayer can submit concrete proof of discovery, the ten-year period is within the control of the government and the taxpayer is at its mercy. The government can always allege any date as the date of its discovery of the falsity, fraud, or omission.

In connection with other violations of the Tax Code, a 5-year prescriptive period is provided under Section 280 thereof. The prescribed 5-year period is counted from the date of the commission of the violation of the law and if the same is not known, at the time of the discovery thereof or the institution of judicial proceedings for its investigation and punishment.

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(b) If before the expiration of the time prescribed in the preceding section for the assessment of the tax, both the Commissioner and the taxpayer have agreed in writing to its assessment after such time, the tax may be assessed within the period agreed upon. The period so agreed upon may be extended by subsequent written agreement made before the expiration of the period previously agreed upon.

(c) Any internal revenue tax which has been assessed within the period of limitation above-prescribed may be collected by distraint or levy or by a proceeding in court within three years following the assessment of the tax.

(d) Any internal revenue tax which has been assessed within the period agreed upon as provided in paragraph (b) hereinabove may be collected by distraint or levy or by a proceeding in court within the period agreed upon in writing before the expiration of the three-year period. The period so agreed upon may be extended by subsequent written agreements made before the expiration of the period previously agreed upon.

(e) Provided, however, that nothing in the immediately preceding section and paragraph (a) hereof shall be construed to authorize the examination and investigation or inquiry into any tax returns filed in accordance with the provisions of any tax amnesty law or decree. (As amended by BP Blg. 700)

## REMEDIES OF THE TAXPAYER

No matter how well or how honestly the books of accounts and records are kept, chances are that there will be a deficiency finding by the BIR examiners.

Without insinuating or adverting to corrupt objectives, I would attribute this more to the old system in the BIR of giving merit to an assessment and not to what is actually collected out of an assessment. Examiners have gotten used to fortifying their merits by showing huge assessments that are not quality assessments at all.

Under these circumstances, it is very important for a taxpayer or corporate officer to know the rights and remedies relative to a proposed deficiency assessment and a formal or official deficiency assessment.

So let us now discuss the remedies before payment of the tax.

## REMEDIES BEFORE PAYMENT OF THE TAX

The remedies of the taxpayer before payment of the tax have two stages: (a) the administrative stage; and (b) the judicial stage.

Administratively, a taxpayer may contest or protest the assessment issued by the BIR with the BIR itself.

At this point, in order to present a more clarified view on the matter, a brief distinction between a proposed assessment and a formal or official assessment, shall be presented.

A proposed assessment is one that notifies the taxpayer of the findings of the examiner. After examination, the examiner submits his recommendation. If he recommends a deficiency assessment, the same is communicated to the taxpayer by the Bureau. The taxpayer is given usually 10 days from notice within which to explain his side. This notice to the taxpayer is a "proposed assessment". This should be distinguished from handwritten or typewritten statements of liability prepared by the examiner which he submits to the taxpayer, usually for purposes of enticing the taxpayer to fix the matter with him. If the taxpayer fails to respond or answer the notice or proposed assessment or even if he responds, if the Commissioner is not satisfied with the taxpayer's explanation, then the Bureau issues an official assessment. For our purposes hereafter when I speak of "assessment" it refers to the latter, meaning, the official assessment as distinguished from a mere proposed assessment.

In contesting or protecting an assessment, the taxpayer must indicate in his protest in detail his basis or reasons for contesting the assessment. The protest must be lodge or filed with the BIR division or department that prepared and issued the assessment. In the case of assessments issued by the



BIR National Office, the assessment for deficiency income tax is prepared and issued by the Sector Operations Service or Department after appropriate review, for specific taxes by the Specific Tax Department, and for the Regional Office by the Regional Director or the National Assessment Service after review and preparation by the National Audit Review Division.

It is important to note that in contesting or protesting an assessment, the protest should not be merely sent through a messenger who files and leaves the same with the division concerned. Sending or filing a protest by mail should also be avoided. One must see to it and be sure that one's protest is attached to or incorporated with the Bureau's docket of the assessment. Otherwise, the division which has one's records may not be the division where one filed his protest. The division that issued the assessment and having possession of one's records might conclude that one has not contested or protested the assessment and the same has become final, thus giving them the right to initiate collection proceedings against him, i.e., issuance of warrants of distraint and levy.

Under the BIR's internal procedure, upon issuance of the assessment, the record or docket of the case is forwarded to the BIR's Receivable Accounts Division to record the assessment or the amount thereof as a receivable. The records are then forwarded to the Collection Enforcement Division the main function of which is to prepare and issue warrants of distraint and levy and garnishment.

The taxpayer should be certain, therefore, that when his case is filed, the records of his case are pulled out of this division (Collection Enforcement Division) and forwarded to the division who will study and resolve his protest. Normally, it is the division that initiates the assessment. If a warrant of distraint and levy is issued against taxpayer, even though his protest has not been studied and considered, this is equivalent to a denial of the protest. In other words, the issuance of the warrant constitutes a decision of the Commissioner on the protest which has to be appealed to the Court of Tax Appeals (CTA) within 30 days from receipt.

It is also indispensable that the taxpayer files his protest within 30-days from receipt of the assessment. If he cannot file a detailed protest within the 30-day period, he must at least file a general or basic protest within said 30-day period requesting for additional time within which to file a supplemental memorandum after he has gone over the details of the assessment based on the records of the BIR which in the same basic protest he will request to be made available to himself. If this is not done, the Commissioner, on the strength of Section 229<sup>6</sup> of the Tax Code, can treat the assessment as final

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<sup>6</sup> SEC. 229. *Protesting of assessment.* — When the Commissioner of Internal Revenue or his duly authorized representative finds that proper taxes should be assessed, he shall first notify the taxpayer of his findings. Within a period to be prescribed by im-

and executory and he can already proceed with the collection of the amount assessed by judicial action. Furthermore, the failure to contest or protest an assessment within the 30-day period would deprive the taxpayer the right to go to the CTA because only decisions of the Commissioner on contested or disputed assessments may be elevated to the court.

In counting the 30-day period for filing a protest against an assessment, I would like to emphasize the importance of indicating in the envelope or in the assessment notice itself the date of receipt thereof. This has to be done by the personnel in one's firm assigned to receive the mail.

If the protest raises questions of facts, it may be assigned for reinvestigation. If it raises questions of law, it will be endorsed for study by the Legal Service Department and the Law Division, now called the Legislative and Research Division of the BIR. Within this department and/or division the taxpayer can follow up and argue the legal points of his case. In all cases, he must be given the opportunity to explain his side.

If, after all these, the protest is denied, the next remedy would be to elevate the case to the Court of Tax Appeals.

However, before appealing to the CTA, the taxpayer may still request the Commissioner for a reconsideration of his decision and ask that his case be referred to the Bureau's Appellate Division, which operates like a court, where both parties are given the chance to present their sides and evidences before a Hearing Officer. This Hearing Officer will later submit his recommendation or decision on the case.

In filing a request for reconsideration the taxpayer must be certain that his request is not merely dilatory or *pro forma*. In other words, he must be able to show that his request for reconsideration raises new issues or arguments or new factual situations other than those covered by his protest. Otherwise, the 30-day period, counted from the Commissioner's denial of the protest within which to appeal the case to the CTA, will not be suspended. In this case, the right to appeal to the court might be time-barred. Only a meritorious motion for reconsideration can stop the running of the 30-day period to appeal to the CTA.

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plementing regulations, the taxpayer shall be required to respond to said notice. If the taxpayer fails to respond, the Commissioner shall issue an assessment based on his findings.

Such assessment may be protested administratively by filing a request for reconsideration or reinvestigation in such form and manner as may be prescribed by implementing regulations within thirty (30) days from receipt of the assessment; otherwise, the assessment shall become final and unappealable.

If the protest is denied in whole or in part, the individual, association or corporation adversely affected by the decision on the protest may appeal to the Court of Tax Appeals within thirty (30) days from receipt of the said decision; otherwise, the decision shall become final, executory and demandable.

I would like to emphasize that the Department or the Secretary of Finance has no power to review, revise or reverse the decision of the Commissioner of Internal Revenue. The Commissioner's decision is reviewable or reversible only by the CTA.

### WAIVER OF THE STATUTE OF LIMITATIONS

Relative to the 3-year period within which the BIR may issue a valid assessment, the examiners may find themselves without enough time to complete an exhaustive examination in view of the impending expiration of the 3-year period to make a valid assessment. In this case, the examiners may rush the preparation of their report to meet the deadline and therefore, force the BIR to issue what is called a "jeopardy assessment." This means there is no well-studied or thoroughly conducted investigation. The examiners may not even have looked into the books of accounts of the taxpayer. An assessment will be made only to beat the deadline for issuing a valid assessment.

To avoid the issuance of a jeopardy assessment, the taxpayer may be requested to execute the Waiver of the Statute of Limitations form, wherein the taxpayer will indicate his conformity to waive the period within which the BIR must issue a valid assessment by indicating an extension of the said period.

The execution of the Waiver may also be required where, after the taxpayer has contested the assessment, there is not enough time within which the examiners can study the protest in view of the impending expiration of the 3-year period within which to collect the tax. Without a waiver, the Bureau may just resort to the summary remedies in collecting the tax which would then be considered as the denial of the taxpayer's protest which has not been studied at all. This could be cured by the filing of the Waiver of the Statute of Limitations extending the period within which the Commissioner may collect the tax.

In this connection, please remember that the Waiver of the Statute of Limitations is valid only if it is executed before the period to be extended lapses. In other words, a Waiver executed after the lapse of the period sought to be extended is not a valid Waiver and could not therefore extend the period to assess and/or collect.

### APPEAL TO THE COURT OF TAX APPEALS

As I mentioned before, the Commissioner's decision on disputed assessments may be appealed to the Court of Tax Appeals which would have to be done within 30 days from the date of the taxpayer's receipt of the Commissioner's decision.

What is appealable to the court is the Commissioner's decision on a disputed assessment. An assessment, if not disputed or contested, may not be appealed to the Court of Tax Appeals.

As previously mentioned, the writ of injunction is ordinarily not available to restrain or prohibit the collection of taxes, so much so, that the Commissioner, upon denial of the taxpayer's protest, would proceed in enforcing the assessment by civil or judicial remedies. However, if an appeal has already been made to the CTA, the said court, as specifically authorized by the law creating it, may issue a writ of injunction to stop the Commissioner from collecting the tax. The writ of injunction therefore is merely an ancillary remedy to an appeal to the CTA. The requirements for the issuance of an injunction by the Court are:

1. The collection of the tax may jeopardize the interest of the government and/or the taxpayer; and
2. The amount claimed must be deposited to the court or a surety bond is filed by the taxpayer for not more than double the amount of the tax assessed.

If not satisfied with the CTA's decision, the taxpayer may still appeal to the Supreme Court within thirty (30) days from receipt of the CTA's decision.

Remember, the 30-day period to appeal to the CTA and to the Supreme Court is jurisdictional and may not be extended even by the courts.

### **REMEDY AFTER PAYMENT**

If payment of the tax has already been made, the taxpayer's remedy is to file a claim for refund/tax credit for erroneously or illegally collected taxes. The claim for refund must be filed with the Commissioner of Internal Revenue to afford him an opportunity to correct his mistake.

Always remember that as required by the Tax Code, a claim for refund must be filed with the Commissioner within two years from payment of the tax sought to be refunded. If the tax is payable in installments, the two-year period is counted from the date of payment of the last installment.

If a claim is not filed with the Commissioner within the two-year period, the taxpayer cannot go to court and he loses his right to the refund/tax credit.

The Tax Code also requires that the claim for refund be elevated to the CTA within the two-year period. Otherwise, the court may not entertain the claim.

The taxes sought to be refunded need not be paid under protest or duress.

One will note that the claim must be elevated to the court within a two-year period, otherwise, the court may not entertain the claim.

Now, how does one reconcile this two-year period with the 30-day period for elevating the claim for refund to the Court of Tax Appeals? In other words, if the taxpayer files a claim for refund and the Commissioner has not yet rendered his decision on this claim, may the taxpayer go to CTA?

The applicable laws provide for two periods to be reckoned with — the 30-day period to appeal a decision of the Commissioner and the two-year period within which to appeal to the court. Which should prevail? Or should both be reconciled and complied with?

This dilemma has been resolved by the Supreme Court in its leading decision in the case of *Muller & Phipps vs. The Commissioner of Internal Revenue*.<sup>7</sup> In this case, the court ruled that if the two-year period is about to lapse and the Commissioner of Internal Revenue has not yet decided the claim, then the taxpayer, without awaiting the decision of the Commissioner, may elevate the claim to the Court of Tax Appeals to comply with the two-year period requirement.

However, if the Commissioner decides the claim within the two-year period and the 30-day period within which to appeal falls within or is covered by the two-year period, the claim should be elevated to the Court of Tax Appeals within the 30-day period. If part of the 30-day period falls beyond the two-year period, then the claim must be elevated within the portion of the 30-day period falling within the two-year period.

Supposing a taxpayer, after receiving an assessment, did not contest the assessment within the prescribed period and therefore losing the right to appeal against the assessment of the Commissioner. May he then pay the tax and afterwards claim refund thereof, alleging that the tax was erroneously or illegally collected?

In a leading decision, the Supreme Court said, "No." According to the Court, if this is allowed, the taxpayer will in effect be authorized to circumvent the law and the 30-day period to appeal the decision of the Commissioner on a disputed assessment will be rendered meaningless.

### NON-RETROACTIVITY OF RULINGS

Another provision of the Tax Code which the taxpayer should remember and keep as part of his stock of remedies is Section 246<sup>8</sup> of the Tax Code

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<sup>7</sup> 103 Phil 145.

<sup>8</sup> Non-retroactivity of rulings. — Any revocation, modification or reversal of any of the rules and regulations promulgated in accordance with the preceding section or any of

which provides for the non-retroactivity of rulings of the Commissioner that reverse previous rulings issued by him if the reversing ruling would prejudice the taxpayer.

An example of this is in the case where a taxpayer who is starting a business operation and not knowing the tax liabilities or taxes that he has to pay in connection with his business operations goes to the BIR and requests for a ruling, setting the facts covering his business operations and asking the Commissioner what tax or taxes he has to pay in connection therewith. If the Commissioner, after answering the taxpayer and enumerating the taxes he has to pay, comes around several years after and, without any changes in the tax laws, says that the taxpayer has to pay some other kinds of taxes which are larger or imposing higher amounts than what was stated in his previous ruling, that late ruling will be a reversal of the original ruling obtained by the taxpayer and will prejudice the taxpayer. In which case the latter cannot give retroactive effect but only prospective effect thereon.

With all these discussions, hopefully, taxpayers and responsible tax officers of respective companies, will now be armed with the necessary remedies to repel and defend oneself and one's respective companies from any improper assessments and actions of the Bureau of Internal Revenue.

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the rulings or circulars promulgated by the Commissioner shall not be given retroactive application if the revocation, modification, or reversal will be prejudicial to the taxpayers except in the following cases: (a) where the taxpayer deliberately misstates or omits material facts from his return or in any document required of him by the Bureau of Internal Revenue; (b) where the facts subsequently gathered by the Bureau of Internal Revenue are materially different from the facts on which the ruling is based; or (c) where the taxpayer acted in bad faith.