

THIRD DIVISION

[G.R. No. 232663, May 03, 2021]

COMMISSIONER OF INTERNAL REVENUE, PETITIONER, VS. SPOUSES REMIGIO P. MAGAAN AND LETICIA L. MAGAAN, RESPONDENTS.

DECISION

LEONEN, J.:

Due process requires that taxpayers be sufficiently informed of the factual basis for the allegation of fraud in the filing of their tax returns. Assessments must be based on facts and not mere presumptions. A taxable partnership has a separate juridical personality from its partners and is liable for income taxation. Without clear and convincing proof that the taxpayers received taxable income personally, or through the partnership, no intention to evade payment of taxes may be inferred.

This Court resolves a Petition for Review on Certiorari^[1] assailing the Decision^[2] and Resolution^[3] of the Court of Tax Appeals *En Banc*, which reversed the Decision^[4] and Resolution^[5] of the Court of Tax Appeals Second Division. In so ruling, it cancelled the deficiency assessments for income and percentage taxes against Remigio and Leticia Magaan (the Magaan Spouses) for 1998, 1999, and 2000.

On November 9, 2005, a confidential informant filed a ComplaintAffidavit before the Bureau of Internal Revenue. They alleged that since 1998, the Magaan Spouses had been operating two financial companies, Imilec Tradehaus and Services Company (Imilec Tradehaus) and L4R Realty and Development Corporation (L4R Realty). The confidential informant reported that the spouses allegedly earned P35,498,477.62 from April 1998 to January 2002, but this income was not declared in their income tax returns.^[6]

On February 9, 2006, the Bureau of Internal Revenue issued a Letter of Authority for the examination and audit of the Magaan Spouses'/Imilec Tradehaus's books of accounts and other accounting records for internal revenue taxes covering taxable years 1998 to 2001.^[7]

On February 28, 2006, the Magaan Spouses were given a Final Notice to present their books of accounts and other accounting records to the investigating team not later than 10 working days from receiving the notice.^[8] Thereafter, a Notice for an Informal Conference was issued.^[9] The Magaan Spouses also received a Subpoena *Duces Tecum* instructing them to appear before the Chief of the Prosecution Division on July 4, 2006, and to bring books of accounts, tax returns and payments, and other records for taxable years 1998 to 2001.^[10]

Remigio later sent a compliance letter dated July 3, 2006, claiming that they were not involved with Imilec Tradehaus or in any of its business transactions. He attached its Articles of Partnership to prove that they were not partners of Imilec Tradehaus.^[11]

In its September 25, 2006 letter, the Bureau of Internal Revenue refused to give due course to the Magaan Spouses' compliance letter for being belatedly filed. It also denied their allegation that they were not connected with Imilec Tradehaus, noting that the spouses continued the partnership's lending operations after its legal existence had been terminated on February 16, 1999. It gave the spouses another five days to comply with the Subpoena.^[12]

On June 20, 2007, the Bureau of Internal Revenue issued a Preliminary Assessment Notice assessing deficiency income and percentage taxes from 1998 to 2000, respectively amounting to P20,773,278.63 and P1,981,362.40. Allegedly, the undeclared income was based on the checks issued to the Magaan Spouses, which were undeclared for that period.^[13]

For their failure to comply with the Subpoena, the Bureau of Internal Revenue filed two Complaints against the Magaan Spouses for violation of Section 266, in relation to Section 5 of the National Internal Revenue Code.^[14] Upon the Office of the Prosecutor's finding of probable cause,^[15] an Information was filed before the Metropolitan Trial Court.^[16]

On October 16, 2007, the Magaan Spouses sent a letter questioning the basis of the Preliminary Assessment Notice. They requested copies of the checks and the documents linking them to Imilec Tradehaus.^[17]

Instead of the requested documents, the Magaan Spouses received a tabular summary of check payments with the payee, the amounts, and the banks where the checks were deposited.^[18] It included a detailed computation of their income and percentage tax liabilities based on the check payments.^[19]

On November 13, 2007, the Magaan Spouses reiterated their request for copies of the actual documents because the summaries furnished to them were "inadequate and confusing."^[20] Allegedly, the computations stated in these documents resulted in greater tax liabilities than those stated in the Preliminary Assessment Notice.^[21]

The Bureau of Internal Revenue denied their request for copies of the checks because the identity of the informer would be revealed.^[22] The Magaan Spouses asked for reconsideration, arguing that the identity of the informant had already been disclosed in the joint resolution in the criminal case filed against them.^[23]

On July 28, 2008, the Bureau of Internal Revenue issued the Formal Letter of Demand with Audit Result/Assessment Notices.^[24] The deficiency income taxes, surcharges, and interests were as follows:

| Year | Basic | Surcharge | Interest | Total |
|----------------------|--------------|------------|--------------|--------------|
| 1998 ^[25] | 1,541,319.00 | 770,659.50 | 2,851,440.15 | 5,163,418.65 |

| | | | | |
|----------------------|--------------|--------------|--------------|---------------|
| 1999 ^[26] | 4,850,045.13 | 2,425,022.57 | 8,042,991.51 | 15,318,059.21 |
| 2000 ^[27] | 585,632.96 | 292,816.48 | 854,048.06 | 1,732,497.51 |

Meanwhile, the deficiency percentage taxes, surcharges, and interests were as follows:

| Year | Basic | Surcharge | Interest | Total |
|----------------------|------------|------------|------------|--------------|
| 1998 ^[28] | 145,860.00 | 72,930.00 | 274,703.00 | 493,493.00 |
| 1999 ^[29] | 450,105.92 | 225,052.96 | 757,678.30 | 1,432,837.18 |
| 2000 ^[30] | 63,385.50 | 31,692.80 | 94,021.83 | 189,100.13 |

On August 26, 2008, the Magaan Spouses filed a letter protesting the Formal Letter of Demand.^[31]

On January 5, 2009,^[32] the Magaan Spouses received the Final Decision on Disputed Assessment, where the Bureau of Internal Revenue denied their protest for lack of factual and legal bases. The spouses were assessed a total of P24,329,405.68 worth of deficiency taxes inclusive of surcharge and interests.^[33]

On February 3, 2009, the Magaan Spouses filed a Petition for Review^[34] before the Court of Tax Appeals. In turn, the Commissioner of Internal Revenue filed an Answer. After pre-trial, trial ensued.^[35]

On November 17, 2009, the Magaan Spouses presented their evidence and filed their formal offer. The Court of Tax Appeals Second Division admitted their exhibits except for the original documents they failed to present.^[36]

Meanwhile, the Commissioner of Internal Revenue submitted the affidavit of Yolanda G. Maniwang (Maniwang). The spouses opposed her presentation as a witness because she was the confidential informant whose participation in the proceedings should have ended upon the submission of the investigation report. Maniwang's testimony was, however, eventually allowed to be presented.^[37]

The Commissioner of Internal Revenue later submitted its Formal Offer of Documentary Evidence. All but the photocopied exhibits of the check payments were admitted.^[38] The Commissioner moved to set a hearing to mark the originals and to file a supplemental formal offer of evidence: This was granted and the exhibits were marked as faithful copies of the original. However, the Commissioner failed to file a supplemental formal offer, and was deemed to have waived the right to do so.^[39]

The parties were directed to file their memoranda, but only the Magaan Spouses filed their Memorandum.^[40]

In the March 9, 2015 Decision,^[41] the Court of Tax Appeals Second Division denied the Magaan Spouses' Petition for Review. The dispositive portion reads:

WHEREFORE, premises considered, the instant Petition for Review is **DENIED**. Accordingly, petitioner spouses are liable for deficiency income tax and percentage tax for the years 1998, 1999 and 2000 in the aggregate amounts of P9,900,203.90 and P1,560,465.22, respectively,

inclusive of the 50% surcharge imposed under Section 248(B) of the NIRC of 1997, summarized as follows:

| DEFICIENCY INCOME TAX | | | |
|------------------------------|----------------------|----------------------|----------------------|
| Taxable Year | Basic Tax | Surcharge | Total |
| 1998 | P1,171,570.00 | P585,785.00 | P1,757,355.00 |
| 1999 | 5,282,006.54 | 2,641,003.26 | 7,923,009.80 |
| 2000 | 146,559.40 | 73,279.70 | 219,839.10 |
| Total | P6,600,135.94 | P3,300,067.96 | P9,900,203.90 |

| DEFICIENCY PERCENTAGE TAX | | | |
|----------------------------------|----------------------|--------------------|----------------------|
| Taxable Year | Basic Tax | Surcharge | Total |
| 1998 | P188,725.00 | P94,362.50 | P283,087.50 |
| 1999 | 815,625.24 | 407,812.62 | 1,223,437.86 |
| 2000 | 35,959.90 | 17,979.96 | 53,939.86 |
| Total | P1,040,310.14 | P520,155.08 | P1,560,465.22 |

In addition, petitioner spouses are liable to pay:

(a) Deficiency interest at the rate of twenty percent (20%) per annum pursuant to Section 249(B) of the NIRC of 1997, as amended, on the:

1. basic deficiency income taxes of P1,171,570.00, P5,282,006.54 and P146,559.40 for the years 1998, 1999 and 2000, respectively, computed from April 15, 1999, 2000 and 2001 until full payment thereof; and
2. basic deficiency percentage taxes of P188,725.00, P815,625.24 and P35,959.90 for the years 1998, 1999 and 2000, respectively, computed from January 25, 1999, 2000 and 2001 until full payment thereof; and

(b) Delinquency interest at the rate of 20% per annum on the total amounts due of P9,900,203.90 and P1,560,465.22 representing deficiency income tax and percentage tax, respectively and. on the deficiency interest which have accrued as aforesaid in (a) computed from January 5, 2009 until full payment thereof, pursuant to Section 249(C) of the NIRC of 1997, as amended.

SO ORDERED.^[42] (Emphasis in the original, citation omitted)

The Court of Tax Appeals Second Division held that the Magaan Spouses may be held liable based on Maniwang's confidential information.^[43] It found that the spouses received income from the checks issued by Maniwang, but these were not declared in their tax returns from 1998 to 2000.^[44] Even if the checks were not formally offered in evidence, these were deemed to have been duly identified by Maniwang, originally marked, and incorporated in the case records.^[45]

The Second Division also observed that the check payments corresponded to the restructured loan stated in the Real Estate Mortgage that Remigio Magaan, Rubilina M. Simbulan, and Roselita M. Joanino executed with Maniwang and her husband.^[46] Since there was a restructured loan, the Second Division concluded that a loan must have existed before the Real Estate Mortgage was executed on October 6, 1999.^[47] Considering the Magaan Spouses' failure to refute the evidence against them, it held them liable for deficiency income and percentage assessments, surcharge, and interests based on the total amount of the checks.^[48]

In its June 30, 2015 Resolution,^[49] the Court of Tax Appeals Second Division denied the Magaan Spouses' Motion for Reconsideration.

On August 11, 2015, the Magaan Spouses filed a Petition for Review before the Court of Tax Appeals *En Banc*.^[50]

In a January 11, 2017 Decision,^[51] the Court of Tax Appeals *En Banc* reversed the Second Division's rulings. The dispositive portion reads:

WHEREFORE, premises considered, the Petition for Review filed by Spouses Remigio P. Magaan and Leticia L. Magaan is hereby GRANTED. The Decision dated March 9, 2015 and the Resolution dated June 30, 2015 are **REVERSED** and **SET ASIDE**. Consequently, Assessment Nos. ES-IT-1998-0699, ES-PT-1998-0700, ES-IT-1999-0701, ES-PT-1999-0702, ES-IT-2000-0703 and ES-PT-2000-0704 are **CANCELLED**.

SO ORDERED.^[52] (Emphasis in the original)

The Court of Tax Appeals *En Banc* held that since fraud was not proven, the Second Division erroneously applied the 10-year prescription period.^[53] It held that the spouses were assessed as if they filed no return; when in fact, as found by the Second Division, the Bureau of Internal Revenue had issued a certification that they did so.^[54]

The *En Banc* also ruled that the Commissioner of Internal Revenue failed to prove that the Magaan Spouses intentionally evaded payment of correct taxes.^[55] The Commissioner was not able to present adequate proof that they owned and operated Imilec Tradehaus, or that its registered partners were the spouses' dummies.^[56] It also failed to prove that the bank accounts in which the checks were deposited belonged to the spouses. The *En Banc* noted that Maniwang had admitted having no proof that the account numbers actually belonged to the spouses.^[57]

The *En Banc* then declared the assessments void for lacking factual and legal bases.^[58] It observed that there were no details in the Formal Letter of Demand elaborating how the assessed amount was computed.^[59]

Finally, the *En Banc* did not apply the disputable presumption that assessments are correct, noting that the assessment of deficiency income and percentage taxes are unfounded.^[60]