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## **TOP OF MIND**

By **LEAH FRANCESCA M. CASTILLO**

# Challenging the merit of presumed regularity

Adjunct to the presumption of regularity in the performance of official duties is the presumption of correctness of a tax assessment. Well-established is the rule in taxation that assessments are prima facie presumed correct and made in good faith. An assessment fixes and determines the tax liability of a taxpayer. As soon as it is served, the taxpayer concerned is supposed to be obligated to pay the amount assessed and demanded.



Although the presumption of regularity of assessments is expressed in a language

superior and demanding, the power that shields an assessment is not without limits. It actually imposes a great responsibility on the tax authorities to ensure that every assessment wears the badge of credibility and due diligence.

In the ordinary course of audit examinations, table audit is the preliminary step to determine whether there arises a questionable item of taxation that needs to be included in an assessment. There is no doubt that it is most convenient to spot discrepancies and inconsistencies when comparing returns and financial statements. However, it is common to see some examiners from the Bureau of Internal Revenue (BIR) resort to include items of discrepancy in tax assessment based only on table audit investigations without further examinations. Nevertheless, there are more instances where an immediate inquiry on the financial statements would already settle the issue of the discrepancy, thus avoiding the need to include the items in the assessment.

On-the-surface discrepancies are manifest in table audit assessments. Perhaps the much too often observable reliance of tax authorities on the strength of the presumption of regularity has compromised credibility for expediency. As a result, the amounts are often too incredible, fantastic and sometimes worse, they are used as a leverage in protests.

We do not immediately fixate a lack of prudence on the part of tax authorities but the prevalence of the said practice has supported the proposition that the assessments may be conducted ineffectively. The reliance on such presumption is somehow abused and has seemed to cause a public discredit

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against tax authorities.

In order to strike the balance between the duty of the tax authorities to assess and collect the right amount of taxes and the right of the taxpayers to due process and property, the courts have weighed in on such presumption.

Since the presumption of regularity is disputable, it can be defeated by proof that the assessment is utterly without foundation, arbitrary and capricious. As such the Supreme Court said that where the BIR has come out with a "naked assessment," i.e., without any foundation character, the determination of the tax due is without rational basis. In such a situation, the determination of the Commissioner of Internal Revenue contained in a deficiency notice disappears (Commissioner of Internal Revenue vs. Hantex Trading, G.R. No. 136975, March 31, 2005). Hence, the determination by the courts must rest on all the evidence introduced and its ultimate determination must find support in credible evidence. Assessments should not be based on mere presumptions no matter how reasonable or logical said presumptions may be. (Collector of Internal Revenue vs. Benipayo, G.R. No. L-13656, Jan. 31, 1962)

As such, the question that arises is: Is a showing of a discrepancy sufficient to warrant a valid assessment?

In the recent Court of Tax Appeals (CTA) case of BPI Capital Corp. vs Commissioner of Internal Revenue (CTA Case No.8787, July 12, 2016), the finding on the unexplained source of cash was dependent on the difference between the total of the salaries and wages reflected in the petitioner's trial balance, financial statements, income tax returns and the Alphalist of employee's compensation. This position of the BIR was rejected by the CTA citing the case of the Benipayo case above: "Assessments should not be based on mere presumptions no matter how reasonable or logical said presumptions may be. In order to stand the test of judicial scrutiny, the assessment must be based on actual facts. The presumption of correctness of assessment being a mere presumption cannot be made to rest on another presumption."

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The CTA does not intend to discount the sound judgement and capability of tax authorities in their functions. The CTA only demands that actual facts be acquired and inquired further should a potential tax exposure arise out of mere logical inference.

Take the case of Spouses Pacquiao vs CIR, (G.R. No. 213394, April 6, 2016), the petition was remanded to the CTA to conduct a preliminary hearing, to determine, among other things, whether the Formal Letter of Demand (FLD) against petitioners was irregular, as it allegedly stated that the amounts therein were “estimates based on possible sources.”

Similar to the findings of the CTA, the court held that “a taxpayer should be informed in writing of the law and the facts on which the assessment is made, otherwise, the assessment is void. An assessment, in order to stand judicial scrutiny, must be based on actual facts. The assertion that the assessment of the CIR was not based on actual transactions but on ‘estimates based on best possible sources’ merit the need for the CTA to conduct a preliminary hearing.”

Mere reliance on “estimates based on best possible sources” casted doubt on the presumption of regularity. Consequently, the CTA was ordered to determine whether these sources are substantial to merit regularity in the issuance of the FLD against spouses Pacquiao.

Apart from the enjoyment of presumption of regularity, tax authorities have an enormous power to seek evidence outside of the documents filed by the taxpayer, i.e. third-party information. There is no excuse for a BIR examiner not to acquire and present evidence manifesting actual facts on which the assessment is based. Further inquiry on matters of dispute is a standard of due diligence which will not only contribute to expediency but will strengthen the credibility of the BIR itself.

Inasmuch as the taxpayer is given the chance to refute the items in an assessment through contrary evidence, an item of taxation once exposed in an assessment will immediately call the attention of tax authorities on the next taxable years and even those prior to it. It would thus be difficult to remove the shadow of doubt casted on the taxpayer with respect to paying the right taxes. As such, even when a taxpayer is compliant, time and effort is taken to prove the tax authorities otherwise.

Be mindful of the fact that a tax assessment is a form of intrusion on an individual’s paramount right to property, presumptions should not be treated as a license to under deliver on the part of the BIR but a seal of credence and reliability.

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