



TAX LAW FOR BUSINESS
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Authority to examine taxpayers' books

By this time, many taxpayers may have already completed their tax obligations for the previous year by filing their annual income-tax returns and paying their income taxes due. But still many others are busy finalizing the documents and other information, which are necessary in the completion of the income-tax return.

Others simply opted to wait for the deadline. Whatever is the reason for not filing earlier, no penalties should follow for as long as the returns and the applicable taxes are filed and paid on or before the deadline.

Filed on time or not, the submission of the income-tax return is not the end of the woes and apprehensions of taxpayers. As so provided under Section 6 of the Tax Code, after a return has been filed, the commissioner or his duly authorized representative may authorize the examination of any taxpayer and the assessment of the correct amount of tax.

The Bureau of Internal Revenue (BIR) usually determines the groups of taxpayers or the industries to be included in the priority list for audit for a specific period. But even if a taxpayer does not belong to this priority audit list, it may still be the subject of an examination. Once a return has been filed, that return and related documents of the taxpayer can be the subject of examination. In fact, failure to file a return does not prevent the commissioner from authorizing the examination of any taxpayer.

But do agents of the BIR have authority to examine records of taxpayers at will and/or without limitation? The Supreme Court in GR 178697, November 17, 2010, said there must be a grant of authority before any officer can conduct an examination or assessment. Equally important is that the revenue officer so authorized must not go beyond the authority given. In the absence of such an authority, the assessment or examination is a nullity.

Thus, it is important to note that the scope of examination should be limited to the authority given in the Letter of Authority (LOA). As described by the court, the LOA is the authority to the appropriate revenue officer assigned to perform assessment functions. It empowers or enables the revenue officer to examine the books of account and other accounting records of a taxpayer for the purpose of collecting the correct amount of tax.

Taxpayers should, therefore, be aware that during the conduct of the examination, the revenue examiners cannot include the examination of books and other accounting records not within the scope and period covered by the authority. In fact the court also noted that the use of the phrase “unverified prior years” as the coverage of the LOA violates Memorandum Order 43-90, which provides that an LOA should cover a taxable period not exceeding one taxable year.

Similarly, in CTA Case 7752, December 21, 2010, which was decided by the Court of Tax Appeals, the court stressed that for an audit and examination of books to be lawful, it must be based on a valid LOA, empowering the assigned revenue officer to examine and scrutinize a taxpayer’s books of accounts and other records to determine tax liabilities. Interestingly, the court also noted that an LOA must be served on the taxpayer within 30 days from the date of issue lest the authority becomes null and void. The revenue officer, on the other hand, has 120 days from receipt of the LOA by the taxpayer, to conduct the examination and inspection.

This case involves an assessment made based on an inventory verification conducted by agents of the BIR. There was no LOA or mission order (MO) issued to the taxpayer for the conduct of the inventory verification. The court ruled that an inventory verification cannot be deemed lawful absent a mission order and a letter to the taxpayer, both of which must be signed by the assistant commissioner, Large Taxpayers Service or the concerned regional director.

Clearly, while the BIR has the power to conduct the audit and investigation of records of taxpayers to determine the correct amount of tax liabilities, the same should be done in accordance with the procedures prescribed by law and the rules promulgated by the BIR itself. An examination should be preceded by a duly issued LOA or MO, and the actual conduct of investigation shall be limited to the persons and the scope specified in said LOA or MO. Absent compliance of these requirements, an examination or investigation may not give birth to a valid assessment.

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