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REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

PAMPANGA SUGAR MILLS,
Petitioner,

- versus - C.T.A Case No. 599

COMMISSIONER OF INTERNAL REVENUE,
Respondent.
x - - - - - - - - - - - - x

10/8/82

D E C I S I O N

This is an appeal from the decision of respondent Commissioner of Internal Revenue dated April 5, 1955 demanding payment of the sum of ₱97,280.00, ₱69,502.00 and ₱12,788.00 as deficiency income taxes for the years 1951, 1952 and 1953, respectively (pp. 241-244, BIR rec.), computed as follows:

1951

Net income per original investigation			₱429,965.30
Deduct:			
Depreciation on new assets acquired from 1946 to 1948		₱56,867.82	
Error in addition		78.92	
Total		₱56,946.74	
Less:			
Bad debts pre-war Planters account	₱157,938.93		
Crop loan	8,790.78		
	₱166,729.71		
Less:			
Mr. Jose Yulo acct.	126,629.76	40,099.95	16,846.79
Net Income per reinvestigation			₱413,118.51
Tax due thereon			₱ 97,280.00

1952

Net income per original investigation		₱412,060.29
Deduct:		
Depreciation on assets acquired in 1947 to 1948	₱ 50,269.87	
Error in addition	7,049.00	57,318.87
Net income per reinvestigation		₱354,741.42
Tax due thereon		₱ 91,327.00
Less: Tax already assessed		21,825.00
Deficiency tax due		₱ 69,502.00

1953

Net income per original investigation		₱284,544.20
Deduct:		
Inventory adjustment	₱171,748.82	
Depreciation on assets acquired from 1946 to 1948	47,691.50	
Error in addition	1,164.20	220,604.52
Net income per reinvestigation		₱ 63,939.68
Tax due thereon		₱ 12,788.00

As borne out by the records, petitioner is a corporation organized and existing under the laws of the Republic of the Philippines. At that time of organization, it has as its principal office at Del Carmen, Floridablanca, Pampanga and was engaged in the milling and processing of sugar into finished products.

In the early part of 1955, an examiner of the Bureau of Internal Revenue investigated petitioner and examined its books of accounts. Accordingly, based on the investigation, respondent wrote petitioner a letter dated April 5, 1955, enclosing therein three assessment notices namely: No. 40-ECAR-5-54-51 for ₱111,491.00; and No. 40-ACR-7-54-52 for ₱85,552.00; and No. 40-FCAR-5-54-53 for ₱71,672.00 (See Annexes "A", "C", & "D", Petition for Review, pp. 12-24, CTA rec.), demanding from the latter the payment of the aforesaid amounts representing the alleged deficiency income taxes due from petitioner for the years 1951, 1952 and 1953, respectively, computed as follows:

1951

Net loss per return		(₱557,922.06)
Add: the following disallowances -		
1. War Damage Losses . .	₱660,150.91	
2. Pre-war loans to planters written off	168,309.48	
3. Depreciation . . .	139,379.57	
4. Loss on sale of assets	20,047.40	987,887.36
Net income as per investigation		₱429,965.30
TAX DUE THEREON		₱111,491.30

1952

Net income as per return	₱106,517.00
Add: Inventory adjustment	171,748.82
Depreciation	132,318.38
Loss on assets fully depreciated .	1,476.09
Net income as per investigation	₱412,060.29
Tax due thereon	₱107,377.00
Less tax already assessed	21,825.00
Deficiency income tax due	₱ 85,552.00

1953

Net loss as per return		(₱ 38,107.00)
Add: Bad debts written off (pre-war account) .	₱188,950.00	
Depreciation	130,515.12	
Undeclared sale of depreciated assets . .	3,186.08	332,651.20
Net income as per investigation		₱284,544.20
TAX DUE THEREON		₱ 71,672.00

Not convinced of the legality of the assessments, petitioner filed a protest with respondent on December 13, 1955 (pp. 293-297, BIR rec.) on the ground that respondent's field examiner has misinterpreted various questions of fact and law with respect to this case, and requesting respondent either to withdraw said assessments, or to instruct his field examiners to conduct a reinvestigation. In a letter dated June 1, 1955 (p. 189, BIR rec.), respondent requested petitioner to execute a waiver on the running of the statute of the limitations up to December 31, 1957, which petitioner did, as evidenced by the waiver petitioner had executed and signed thru its responsible officer. (p. 194, BIR rec.)

On October 18, 1955, after a careful study of the case, respondent wrote a letter to petitioner reducing the assessments of the alleged deficiency income taxes for the years 1951, 1952 and 1953 to ₱97,280.00, ₱69,502.00 and ₱12,788.00, respectively, which revised assessments were received by petitioner on October 18, 1955. (pp. 287-286, BIR rec.)

On December 9, 1955, petitioner again protested the assessments on the ground that the amounts of deficiency assessments were not arrived at by respondent on the bases of a just appreciation of the facts and law involved, and, therefore, requested for another reinvestigation. (pp. 249 to 253, BIR rec.)

Consequently, respondent conducted another reinvestigation and rendered his decision on September 26, 1958 (p. 361, BIR rec.), which was received by petitioner on October 29, 1958.

Respondent, in a memorandum dated June 23, 1958 addressed to the Regional Director, San Fernando, Pampanga (pp. 343-347, BIR rec.) has listed down the disallowed items claimed by petitioner in the taxable years in question.

1 9 5 1

Pre-war planters accounts written off	₱208,409.43
Depreciation on cost of rehabilitation	82,432.83
Loss on sale of asset	20,047.80
War damage losses	660,150.91

1 9 5 2

Depreciation on cost of rehabilitation	₱ 74,999.51
Loss of assets fully depreciated	1,476.09

1 9 5 3

Depreciation on cost of rehabilitation	₱ 81,659.82
Undeclared sale of depreciated assets	3,186.08
Bad debts written off	188,950.00

Respondent, in a letter dated September 26, 1958 (p. 361, BIR rec.), informed petitioner that with regards to its deficiency income tax liabilities for the years 1951, 1952 and 1953 in the total amount of ₱179,570.00 and that after a thorough re-investigation and study of the case, he came to the conclusion that no valid reasons exist to warrant modification of the previous assessment against the petitioner and that petitioner failed to substantiate or justify the aforementioned deductions in its income tax returns for the years 1951, 1952 and 1953.

At this juncture, it should be stated that assessments are presumed to be correct unless the contrary is shown, and the burden of proof rest upon the taxpayer to overcome this presumption. The determination, however, of a deficiency by the government is only <u>prima facie</u> correct. (Gutierrez vs. Collector of Internal Revenue, L-19537, May 20, 1967, 14 SCRA 33; Tan Guan vs. Court of Tax Appeals, L-23676, April 27, 1967, 19 SCRA 903; Republic vs. Philippine Rabbit Bus Line, Inc. L-26862, March 30, 1970, 32 SCRA 211.)

In view of the aforesaid legal presumption and the defense of respondent that the above items of deductions are disallowable because in the two reinvestigations conducted by his office, no justification existed to warrant modification of the questioned deficiency assessment, the court will now proceed to assess the evidence of the parties presented, not only in the hearing before the appellate division of the Bureau of Internal Revenue but also before this Court. We will then determine whether petitioner has properly substantiated his claimed deductions for his 1951, 1952 and 1953 income tax returns. At the outset, hearings before this Court partakes of a trial de novo and shall therefor recieve evidence, summon witnesses, and give both parties, the government and the taxpayer, opportunity to present and argue their sides in order that the true and correct amount of the tax liability may be finally determined and decided. (Collector of Internal Revenue vs. Batangas Transportation Company & Laguna Tayabas Bus Company, L-9692, January 6, 1958, 102 Phil. 822.)

We shall now discuss the disallowed items in the order listed by respondent in his memorandum and ascertain whether or not petitioner is entitled to these deductions.

Petitioner did not go to trial but admitted the findings of facts of the respondent. The issues are as follows:

(a) Whether or not the uncollected portion of pre-war loans is deductible as bad debts for income tax purposes;

(b) Whether or not depreciation of pre-war assets is deductible in any taxable year at the option of the taxpayer;

(c) Whether or not the pre-war losses may be claimed during the taxable years after the war; and,

(d) Whether or not a loss on the sale of fully depreciated capital assets is deductible.

<u>Pre-war Planters Loan written off as bad debts in 1951 - ₱208,409.43</u>

The records show that petitioner granted pre-war loans to the sugar planters numbering, all in all, two hundred thirty four (234) loans. Petitioner alleged that after the war, it exerted efforts to collect said loans. Written demands were made to the planters-debtors. As pointed out by petitioner, it found out later that some of the planters-borrowers were either dead or their whereabouts can not be located. While the others, who survived the war, could not pay because they were victims of the ravages of World War II. Petitioner's unpaid pre-war loans to the planters were written off in 1951 based on its belief that after the war, the planters-debtors were no longer in a position to pay their full indebtedness on account of the widespread, almost complete devastation caused by the war to the nation's productive power. Petitioner claimed that because of this state of affair then existing, it wad confronted with the choice of either retarding the rehabilitation of its business by insisting on complete payment of said loans by the planters-debtors, or to write off the pre-war unpaid loans as bad debts. Petitioner was, therefore, forced by circumstances to implement the second choice, i.e. to consider the pre-war loans to planters as debts which has become bad in 1951. So that in the year 1951, petitioner and some surviving planters entered into a milling contract wherein the indebtedness of the planters were reduced to the extent of the difference between the full pre-war indebtedness and the amount granted as their war damage claim, and that this difference between the full pre-war accounts and their reduced indebtedness is the uncollected accounts and claimed as bad debts.

The provision of the milling contract (p. 6, Petition for Review, p. 6, CTA rec.) entered into by and between petitioners and planters-borrowers contained the following stipulation as herein quoted below:

"4. SETTLEMENTS OF PRE-WAR ACCOUNTS

"It is expressly stipulated that at the outbreak of the war in December, 1941, the PLANTER was indebted to the CENTRAL (petitioner) in the sum of ₱ and it is hereby agreed that said indebtedness of the PLANTER shall be reduced to the total percentage thereof that the war damage commission may be used in the payment of the approved war damage claim. Example: If the total percentage used by the war damage commission in paying war damage claims is 40% of the approved claim, and the recognized pre-war indebtedness of the planters is ₱1,000.00, their said indebtedness shall be reduced to 40% or ₱400.00.

"It is however, expressly stipulated that 4% of the entire sugar production of the plantation to be taken out of the planters' participation shall be retained by the central to be applied to the liquidation of the reduced indetedness of the planters, as herein above provided, until such reduced indebtedness shall have been fully paid."

Petitioner, in support of its contention that the indebtedness written off are allowable, cited Mertens as authority, stating that - "The difference between the face amount of the note and the amount received in compromise is an allowable bad debt deduction, provided the debtor has no assets out of which the entire amount may be collected. The deduction is allowable even though the taxpayer executes releases from the obligation, provided that such releases are executed after bona fide determination of worthlessness by the taxpayer." (Jacob Mertens, Jr. Law of Federal Income Taxation, Vol. 5, 2 Ed. p. 447.)

On the basis of the above provision of the milling contract, petitioner had considered as deductible the difference between the full pre-war indebtedness and the war damage payments to the planters-borrowers as bad debts in the amount of ₱208,409.43.

On the other hand, respondent claims that the amount of ₱208,409.43, representing pre-war accounts to planters written off in the taxable year 1951, should be disallowed as deductible bad debt. Respondent asserts that petitioner failed to substantiate its claim by showing that the planters-debtors were incapable of paying their indebtedness. Respondent alleged that the planters had sufficient income and properties with which to pay their obligations as this was shown by the fact that planters-debtors have executed a new milling contract with the petitioner, and the government had stressed the fact that the debts were even partially settled. (p. 3, Resp's Memo., p. 224, CTA rec.)

We find the contention of respondent untenable. A partially settled debt which has been previously charged off within a taxable year as deductible bad debt can be claimed as deduction in the year it was sustained.

The reporting made by petitioner of income recoveries from bad debts in his subsequent income tax returns, i. e., in 1953, 1954 and 1955 in the amounts of ₱35,168.00, ₱35,168.00 and ₱33,186.00, respectively (p. 345, BIR rec.) will only show that it has no intention to defraud the State of its lawful revenue.

The contention of respondent will not negate the glaring facts clearly in petitioner's memorandum dated June 7, 1978 to the effect that after the war, petitioner had exerted all efforts to collect said loans and that written demands were made to the planters-borrowers for the payment thereof. According to petitioner, many of the planters-borrowers were either dead or could no longer be located. Those planters that survived the war were in no position to meet their obligations on account generally of the almost complete destruction of the nation's productive power of which the planters are not excepted. Petitioner, further, maintained that the inability of the planters-borrowers to pay their obligations was caused by the war, and that despite written demands against the borrowers, no payments were made by them. All these circumstances brought the petitioner to decide and in fact treated the loans as bad debts which it now claims to be deductible as of the year 1951, which this Court finds meritorious. It is a common knowledge that the devastating effects of the last world war to our country's economy is immeasurable. This fact, let alone, supports the validity of the claim of petitioner of its writting off the bad debts for the loans of its pre-war planters in said year.

As admitted by both parties, the debts were incurred before the advent of the Second World War which had been very destructive to many planters and their creditors alike and have adversely affected them both financially. These conditions could not have made possible the early settlement of their indebtedness. Indeed, no one was spared from the ravages and losses caused by the war. In a lesser degree of situation, where a debt was considered worthless, it was taken judicial notice by the Court that a business depression will require a less specific performance to prove that a given debt is worthless." (See Higginbothans Baily Logan, 8 BTA 566, 579.) It was therefore, correct for petitioner to, instead of waiting for an opportunity for these planters to pay their debts which was not then possible, reduce the planter's indebtedness by entering into a new milling contract, and the reduced indebtedness of the planters written off by petitioner as bad debts. And it could not be good management to keep the unpaid accounts alive, which are subject to claims for their payment from year to year, which indeed calls for more expenditures. This Court had ruled, in several cases, that it is foolish to spend good money to recover the bad accounts. And, moreover, in order that a taxpayer may be entitled to deductions, the law does not require him to be an incorrigible optimist. (Goodrich International Rubber Co. vs. Collector of Internal Revenue, CTA Case No. 468, June 8, 1963; G.R. No. L-22265, Dec. 22, 1967, 21 SCRA, modified in G.R. No. L-2265 Dec. 22, 1967, 21 SCRA 1336; El Porvenir Rubber Products, Inc. vs. Vera, CTA Cases Nos. 1702 and 1705, July 26, 1969.)

<u>Bad debts written off in 1953 - ₱188,950.00</u>

Petitioner claimed this amount as bad debts in its income tax return in 1953. This item was disallowed by respondent as shown in his memorandum dated June 23, 1958 addressed to the Regional

Director, San Fernando, Pampanga. (Pp. 345-347, BIR rec.) Respondent, in disallowing the claim for aforesaid bad debt deduction, asserted that the disallowed pre-war accounts should have been written off in the year petitioner started its milling operations.

Respondent also argued that petitioner started milling operations in the year 1947 and it had taken six years to determine whether the debts are collectible or not. Respondent also stated that, in a subsequent reinvestigation made, petitioner had reported as miscellaneous income partial recoveries of these pre-war accounts in the years 1953-55. (p. 345, BIR rec.) Respondent, therefore, insisted that the said accounts should have been written off at the beginning of their operations, i.e., immediately after the war. Bad debts, in order to be deductible, should be actually ascertained to be worthless in a particular year and charged off in that taxable year in its books of accounts, and, that before the debt may be charged off, and consequently deduct said debt, it must be ascertained and demonstrated in a reasonable degree of certainty of the uncollectibility of the debt.

Contrarily, petitioner, in a letter dated December 20, 1955, had clearly shown the validity of its claim for the allowance of bad debts for the taxable year 1953. Petitioner listed down the breakdown of this bad debts items (pp. 299-302, BIR rec.) as follows:

(a) Accounts less than ₱50.00 not circularized	₱ 1,325.42
(b) Account circularized with letters returned marked (deceased) or whereabouts unknown	70,785.04
(c) Accounts circularized with letters received by addressee but no reply received by petitioner	2,374.67
(d) Accounts circularized with letters received and acknowledged by addressee but claiming no indebtedness	102,954.40
(e) Accounts circularized whose letters on which return receipt was not received and have no knowledge if addressee received the letter	2,837.40
T o t a l	₱180,277.18
Plus written off 42% of indebtedness of planters who signed milling contract during 1952-1953	8,672.82
	₱188,950.04

According to petitioner, the items (a) & (b) represent various individual accounts which were quite small, the expenses incurred for the collection of these items would be grossly unproportionate to the amounts to be collected.

Items (c), (d) and (e) represent accounts of debtors whose whereabout are unknown and failed to receive letters of demand. Some of the debtors refused to pay, claiming no indebtedness and some alleging the reasons that they (debtors-planters) do not have any account of fertilizers as no fertilizers were given to them by petitioner and/or that said fertilizer were either taken back by petitioner before the war and which were later confiscated by the Japanese.

Petitioner has ascertained that the inability of the planters-borrowers to pay their obligations consisting of pre-war loans was due to the damages sustained by them during the last war and that despite petitioner's written demands, no payment has been made by them. Petitioner, therefore, concludes that the deductions for bad debt is justified.

This Court finds the contention of respondent untenable. In the first place, respondent's examiner admitted in the reinvestigation report that efforts were indeed exerted by petitioner to ascertain the worthlessness of the debt as shown convincingly in a letter dated December 20, 1955 addressed to respondent Collector (now Commissioner) of Internal Revenue. (pp. 347, 343. BIR rec.) Respondent can not now be allowed to claim that petitioner had failed in its efforts to present evidence showing that the planters-borrowers were indeed incapable of meeting their obligations. Here, it has been shown that the planters' loan accounts were actually and duly ascertained in the year they were claimed as deductible, i.e., in 1951 and 1953 as bad and that these deductions were made in utmost good faith. In the light of the High Court decision, it had ruled thus -

> "xxx Our statute permits the deduction of debts actually ascertained to be worthless within the taxable year; obviously, to prevent arbitrary action by the taxpayer, to unduly avoid tax liability.
>
> The requirement of ascertainment of worthlessness requires proof of two facts: (1) that the taxpayer did in fact ascertain the debt to be worthless, in the year for which the deduction is sought; and (2) that in doing so, he acted in good faith. (Collector of Internal Revenue vs. Goodrich International Rubber Co., 21 SCRA, 1336, 1341.)

As to the claim of respondent that the partial settlement or collection of debts by the debtors-planters are evidence against or deterrents to the deduction of bad debts in the income tax returns of petitioner finds no support in law. This Court held that the subsequent collection of a bad debt previously charged off in a prior year does not render the deduction unallowable.

> Respondent's main argument in disallowing the deduction of the alleged bad debts is that petitioner was able to collect some of the debts or parts thereof in subsequent years, which proved that the debts were not uncollectible in the years they were so declared and charged off by petitioner.
>
> That a debt previously found to be worthless and charged off in a prior year, was subsequently collected does not render the deduction un-unallowable or illegal. (Philippine Trust Company vs. Collector of Internal Revenue, CTA Case No. 367, January 30, 1961.) The taxpayer need not wait uncertain future events, nor wait until some turn of the wheel of fortune may bring the debtors affluence. (Jacob Mertens Jr., <u>Law of Federal Income Taxation</u>, Vol. 5, Chap. 30, p. 123.)

It is the respondent's opinion that the pre-war accounts of the debtors-planters should be written off in the year the company started their milling operations in 1947 or immediately after the war. This claim cannot be sustained. The charging off of a partially worthless debt need not be physically made in the year it becomes worthless. The word "charged-off within the taxable year" in the law refers to and means the state of facts during the taxable year pointing to the uncollectibility of the debts rather than just the requirement of any physical act taken by the taxpayer to collect within that year with respect to the debts. (Jacob Mertens, Jr., Law of Federal Income Taxation, Vol. 5, Chapter 30, p. 36.)

Depreciation allowance for the years 1951, 1952 and 1953 in the respective amounts of ₱82,432.83, ₱74,929.51 and ₱81,659.42.

Petitioner claims that the expenses incurred to rehabilitate its pre-war assets are capital expenditures. Accordingly, to petitioner, standard principles of accounting sanction the depreciation allowances on the said capital expenditures. (Pp. 295-296, BIR rec.) Petitioner further claims that these rehabilitation expenses can be allocated as depreciation allowances to particular group of assets, without proof that the said expenses were in fact used for that respective group of assets to which the depreciation allowances were allocated. (pp. 295-296, BIR rec.) Petitioner argues that to require petitioner to prove that the allocated expenses, which were in fact applied on a group of assets, would be requiring it to perform the most difficult, if not the most impossible thing. In support of petitioner's contention, it cited the following authority:

> "It is not necessary of course to allocate the expenditures in minutiae to each individual piece of property where

> items relates to several depreciating properties, it is sufficient if the expenditures are divided by reasonable apportionment process on a percentage basis among the several properties benefited." (Jacob Mertens, Law of Federal Income Taxation, Vol. 4, p. 60.)

Respondent, in a memorandum dated June 11, 1979, had listed down, in detail (p. 4, Resp. Memo., pp. 225-226, CTA rec.) the following rehabilitation expenses incurred by petitioner on its assets, to wit:

1.	General expenses - various	₱653,937.57
2.	Cost of sale of sugar 60% of the total cost of sale as estimated by the manager	596,195.86
3.	General expenses - various	1,320.27
4.	General expenses - damage	3,986.38
5.	General expenses - club mess	449.71
6.	General expenses - hospital	6,206.46
7.	General expenses - in maintenance in process	54,573.27
	T o t a l	₱1,316,669.47

The above amount of rehabilitation expenses (Pp. 4-5, Resp. Memo, pp. 225-226, CTA rec.) were distributed to the following assets, as per Journal Entry No. 200, on September 20, 1948.

1.	Land improvements	₱4,202.43
2.	Building equipments	268,786.86
3.	Machineries equipment	712,878.70
4.	Railroad equipment	241,829.60
5.	Agricultural Machineries	20,020.82
6.	Furniture & Fixtures	3,932.81
7.	Autotruck travelers	58,223.23
	T o t a l	₱1,316,669.47

On this score, respondent as[illegible] that herein petitioner started milling after the

World War II, or in 1947. Respondent observed that petitioner had capitalized the general expenses by treating the same as rehabilitation expenses and apportioning these expenses to various assets accounts, and depreciated these rehabilitation expenses in accordance with a rate of depreciation for each item. Respondent attacked this procedure, which was adopted by petitioner, and maintained, after reinvestigation, that these general or rehabilitation expenses are not capital expenditures subject to depreciation allowances as these expenses did not increase the value of petitioner's assets. Respondent concludes therefore that the depreciation allowances are improper and cannot be depreciated.

We find the stand taken by petitioner untenable. In the first place, there is no law or jurisprudence which supports the legality of the manner in which petitioner treated, for depreciation allowances purposes, the aforesaid general or rehabilitation expenses. Although it may be said that the rehabilitation expenses partakes of the nature of capital expenditures, it cannot be depreciable unless added to the cost and increasing thereby the value of the assets of petitioner.

> Expenditures may constitute capital investments, but that does not necessarily mean that all capital investment must be included in the capital sum recoverable by depreciation. To be so included, they must either enter into the cost of wasting or depreciating property or must be reasonably attributable to such property (Jacob Mertens, Jr., Law of Federal Income Taxation, Vol. 4, Chap. 23, p. 102.)

The rehabilitation expenses of petitioner not being capital expenditures which increased the value of the company's properties or constitute improvement of the assets to which they are allocated, they can not be allowed as depreciation allowances.

We will now consider the war damage losses in the sum of ₱660,150.91 claimed as deduction in 1951.

In its 1951 income tax return, petitioner claimed as deduction the amount of ₱660,150.91 as war damage losses. Respondent asserted that the losses are deductible only during the taxable years in which these losses were sustained. Respondent cited, in support of his position, the ruling of the Secretary of Justice in Opinion No. 162, series of 1952 dated August 23, 1952 and General Circular No. V-139. Respondent further urge us that the claim of petitioner for deduction for its war losses in 1951 cannot be allowed since these losses were sustained during the Japanese occupation (citing the case of Hilado vs. Coll. of Int. Rev., G.R. No. L-9408, Oct. 31, 1956, 100 Phil. 288) and not in 1951.

This Court finds the respondent's claim of disallowance of the war damage losses in accordance with law. This issue has been squarely settled thus -

> "x x x. The question in regard to the deductibility of war losses has already been settled by the Supreme Court in two cases.
>
> "It has been held that a loss sustained in 1945 as a result of military operations by the United States for the liberation of the Philippines was not compensated for by insurance or otherwise, within the meaning of Section 30(d) of the Revenue Code, and, therefore such loss is deductible only in the year sustained. x x x. (Yulo vs. Araneta, CTA Case No. 84, July 8, 1958; citing Cu Unjieng v. B.T.A., GR No. L-6296. September 29, 1956; Hilado v. Coll. of Int. Rev., 100 Phil. 288, op. cit.) See also Consolidated Mines, Inc. vs. Commissioner, CTA Case Nos. 565 and 578, May 6, 1961.)

Respondent's decision disallowing the war damage losses claimed by petitioner is, therefore, sustained.

Losses on the sale of its assets in the amount of ₱20,047.80 in 1951.

Respondent disallowed this item of ₱20,047.80 allegedly incurred by petitioner on the sale of its assets in 1951 on the ground that said assets at the time of the sale had already been fully depreciated.

Anent this issue, petitioner maintains that normal depreciation cannot be taken against the pwner of the property who had absolutely no control over it. Petitioner further claims that no depreciation should be taken during a forced stoppage in operations occasioned by the war. (pp. 178-179, BIR rec.)

The contention of petitioner is not tenable. In the first place, petitioner failed to substantiate this claim of loss in the sale of its assets. As correctly maintained by respondent, since the assets in question were depreciated when the same was already in use and which depreciation occurred continuously even when idle or temporarily not used, and after having been fully depreciated in value, a sale, thereafter made of the assets will not bring about a loss resulting from the sale subject of claim for allowance. The claim for losses in the sale of the assets in the sum of ₱20,047.80 cannot be sustained.

<u>Losses on the sale of assets fully depreciated in the sum of ₱1,476.09 for 1952.</u>

Again, petitioner claims that normal depreciation cannot be taken against its assets, the same having been in the possession of the Japanese

Forces for which it had no control. We have already decided this in the immediately preceding issue of the deductibility of the loss on the sale of petitioner's asset in the sum of ₱20,047.80. Moreover, where the salvage value plus its depreciation of the asset up to the time of the sale exceeds the properties' selling price, there will be no loss. (Jacob Mertens, Jr., Law of Federal Income Taxation, Vol. 5, Chap. 28, p. 51.) We therefore find respondent's act of disallowing the loss in the sale of depreciated assets in the amount of ₱1,476.09 in 1952 to be correct.

Undeclared sale of depreciated assets in the sum of ₱3,186.08 for the year 1953.

Respondent again contends, just as on the two (2) preceding issues, that in the sale of depreciated assets, loss is not recognized since the investment had been fully recovered by way of depreciation. Respondent maintains, further, that gain may instead be realized as a result of the sale of the depreciated assets.

For the same ground of the disallowance of the losses on the immediately preceding issues, i.e. concerning the disallowance by us of the losses arising from the sale of the assets fully depreciated, we equally uphold respondent's determination that the undeclared sale of depreciated assets in the amount of ₱3,186.08 is not deductible and, hence, includible as income subject to tax for 1953. Accordingly, petitioner's income tax liability for the two years 1951 and 1953 is recomputed as follows:

1 9 5 1

Net loss per return			(₱577,922.06)
Add:			
War damage losses		₱660,150.91	
Depreciation		139,379.57	
Loss on sale of assets		20,047.40	
Total		₱819,577.88	
Deduct:			
Depreciation on new assets acquired from 1946 to 1948	₱56,867.82		
Error in addition	78.92	56,946.74	762,631.14
Net income as per investigation			₱204,709.08
Tax due thereon:			
¼ of ₱204,709.08 = ₱51,177.27 x 16%		= ₱8,188.36	
3/4 of 100,000.00 = ₱75,000.00 x 20%		= 15,000.00	
₱204,709.08 - ₱126,177.27 = ₱78,531.81 x 28%		= 21,988.90	₱45,177.00

1 9 5 3

Net loss per return		(₱38,107.00)
Add:		
Depreciation	₱130,515.12	
Undeclared sale of depreciated assets	3,186.08	133,701.20
Total		₱95,594.20
Deduct:		
Inventory adjustment	₱171,748.82	
Depreciation on assets acquired from 1946 to 1948	47,691.50	
Error in addition	1,164.20	220,604.50
Net loss		(₱125,010.32)

Petitioner is liable for 1952 income tax in the amount of P69,502.00 as determined previously by respondent Commissioner of Internal Revenue.

WHEREFORE, the decision of respondent appealed from is hereby modified. Petitioner is, therefore, ordered to pay the amounts of P45,177.00 and P69,502.00 or a total of P114,679.00 as deficiency income taxes for the years 1951 and 1952 respectively, plus the surcharge and interest which have accrued thereon pursuant to Section 51(e) of the Tax Code as amended.

With costs.

SO ORDERED.

Quezon City, October 8, 1982.

CONSTANTE C. ROAQUIN
Associate Judge

WE CONCUR:

AMANTE FILLER
Presiding Judge

ALEX Z. REYES
Associate Judge