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REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

ASSOCIATED SUGAR, INC.,
Petitioner

versus

CTA CASE NO. 1405

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

April 7/66

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DECISION

This is an appeal from the decision of respondent dated May 29, 1963 holding petitioner liable for the sums of ₱3,256.80 and ₱2,365.90, as deficiency income tax and interest for the years 1958 and 1959, respectively.

The facts of the case are stated in the memorandum of respondent's examiners dated December 10, 1962, from which we quote:

> "The Associated Sugar, Inc. is a duly registered corporation organized since 1948. It was formed primarily for the purposes of 'dealing in wholesale or retail of sugar of all kinds and in goods, wares, or merchandise of any and all kinds and nature whatsoever; and to conduct and carry on any form of mercantile enterprise necessary or incidental to the merchandise business of the company.' It also 'acts as general agents and/or accept agency on commission basis for surety, bond, fire and marine insurance, or for any insurance against any risk of any kind or accident.'
>
> "Subject corporation is one among the many organizations controlled by Mr. J. Amado Araneta, and as such, it acts as the marketing agent of most, if not all, of its sister corporations, specially in the export of sugar. Since it handles a great portion of the business of its affiliated

organizations, more particularly the sugar centrals known as Bacolod-Murcia Milling Co., Talisay-Silay Milling Co., and Ma-aO Sugar Central Co., its books of accounts and accounting records reflect transactions that have direct bearing to these companies. In the course of investigation and examination of its records, some discrepancies affecting its affiliated companies and also their principal stockholder, Mr. J. Amado Araneta, were discovered. These discrepancies were correspondingly reflected in the examiners' report of examination of the taxpayers concerned, whose tax liabilities were also under verification simultaneously with this investigation.

"Aside from these discrepancies affecting its sister companies and principal stockholder, an item which has no relation to its operations but was claimed as a deduction for income tax purposes as 'professional services,' was noted. This item, 'professional services', was the basis of an additional assessment on the taxpayer for the year 1960, after an investigation by Quezon City Internal Revenue Officers. The taxpayer having paid the deficiency tax on this basis has impliedly admitted the impropriety of this deduction, hence, the disallowance of the same item for the years 1958 and 1959. Such item was not claimed in 1961. The foregoing disallowance resulted in deficiency taxes of ₱3,256.80 for 1958 and ₱2,325.80 for 1959, including interests." (See pp. 65-66, BIR rec.)

The deficiency assessment resulted from the disallowance of petitioner's claim for deduction of the compensation paid to Messrs. Jose Ma. Veloso and Horacio Borromeo in the total amount of ₱13,800.00 in 1958 and ₱14,400.00 in 1959 for professional services.

Petitioner also questions the imposition of ½% monthly interest by respondent pursuant to Section 51(d) of the Revenue Code, as amended by Republic Act

No. 2343.

The issue presented for our consideration is whether or not the alleged payments for professional services in the sums of ₱13,800.00 and ₱14,400.00 for the years 1958 and 1959, respectively, are ordinary and necessary expenses paid or incurred in carrying on petitioner's business.

The law applicable is Section 30(a)(1) of the Revenue Code, which provides:

> "SEC. 30. Deductions from gross income.— In computing net income there shall be allowed as deductions -
>
> "(a) Expenses:
>
> "(1) In general.—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; x x x"

There are three conditions for deductibility of a business expense. It must be shown that the expense was (1) incurred in carrying on a trade or business, (2) ordinary and necessary, and (3) paid or incurred within the taxable year (Mertens, The Law of Federal Income Taxation, Vol. 4, par. 25.07, Chap. 25, p. 18; Coll. of Int. Rev. v. The Phil. Education Co., Inc., L-8505, May 30, 1956). There is no dispute that the questioned amounts were paid to Messrs. Horacio Borromeo and Jose Ma. Veloso as public relations officer and financial advisers, respectively, of petitioner during the years in question (Exhs. A to O, pp. 16-

140, CTA rec.).

It is respondent's theory that the expenses incurred were properly disallowed because they are not ordinary and necessary in the conduct of petitioner's business or trade. It is alleged that these expenditures did not help in the development of the business and neither were they helpful for the purpose of realizing profit or minimizing loss (pp. 160-161, CTA Rec.). In other words, the employment of public relations officer and financial adviser did not in any way help in the promotion and development of petitioner's business (See p. 161, Memo. for respondent; pp. 12, 50, 33, BIR rec.).

This view of respondent, in our opinion, is too strict and technical. Petitioner is engaged in the wholesale and retail of sugar of all kinds and in goods, wares or merchandise of any and all kinds and nature whatsoever. It acts as the marketing agent of its sister corporations, specially in the export of sugar. It also handles a great portion of the business of its affiliated organizations, more particularly the sugar centrals known as Bacolod-Murcia Milling Co., Talisay-Silay Milling Co., and Ma-ao Sugar Central Co. Because of these multifarious business activities, petitioner hired the services of Horacio Borromeo and Jose Ma. Veloso. Mr. Horacio Borromeo, a newspaperman, was employed by petitioner as its public relations officer and also acted as financial adviser to Mr.

Araneta. The nature of his work as testified to by Jose A. Sanchez, petitioner's chief accountant, is as follows:

> "x x x For instance, whenever we had some difficulty with our export license with the Central Bank, he used to follow them up to cut down the red tape. Now, when we needed bottoms for the shipment of sugar, he used to help us to look for bottoms and when we were in need of credit accommodations from banks, he used to help the company secure these credit accommodations and he was also, as I said, advising Mr. Araneta on financial and business matters, like for instance, the forecasting of the market for the price of sugar." (pp. 8-9, t.s.n.)

On the other hand, Mr. Jose Ma. Veloso performed about the same functions as Mr. Borromeo, except the public relations phase which was not handled by him (p. 9, t.s.n.). As financial adviser, he was specifically utilized in following up the transactions of petitioner with banks, government offices and shipping companies (p. 22, t.s.n).

We are convinced that the amounts paid to Messrs. Horacio Borromeo and Jose Ma. Veloso were appropriate and helpful in the development of petitioner's business. The services rendered by them were necessary in carrying on the business of petitioner considering the varied activities it was engaged in. An expense is necessary if it is appropriate and helpful in developing and maintaining the taxpayer's business (General Electric [P. I.], Inc. v. Comm. of Int. Rev., CTA Case 1117, July 14, 1963, not appealed). Besides, modern business trends and practices require good public relations for any kind of business. As marketing agent of several sugar centrals, petitioner has to apply for export licenses with the Central Bank, secure the availability of bottoms for the shipment of sugar, and the availability of credit accommodations from banks to finance the exports of its principals. Needless to say, these activities cannot be said to have no direct bearing nor relation to the conduct or operations of petitioner's business. That petitioner incurred losses in some years despite the services of Messrs. Borromeo and Veloso does not mean that the salaries paid to them were not ordinary and necessary in the conduct of its business. In order that the taxpayer's activities may constitute the carrying on of a "trade or business," it is not essential that the net result be profit. It is enough that the enterprise be conducted in good faith with an intention of making a profit or of producing income. The element of profit is only significant insofar as it affords a means of distinguishing between an enterprise carried on in good faith as a "trade or business" and an enterprise merely carried on as a hobby (Mertens, The Law of Federal Income Taxation, Vol. 4, par. 25.08, Chap. 25, p. 21).

Anent the contention of respondent that petitioner impliedly admitted the validity of the herein disallowances when it paid in 1960 the deficiency income tax resulting from the disallowance of ₱15,000.00, representing similar payment for professional services, suffice it to say that payment in a previous year does not preclude a taxpayer from questioning the correctness of similar payments in future years. The fact that petitioner protested the assessment under review is a clear indication that it considered as erroneous its previous decision to pay deficiency income tax on similar disallowances.

IN VIEW OF THE FOREGOING CONSIDERATIONS, the assessment appealed from is hereby reversed and set aside, without pronouncement as to costs.

SO ORDERED.

Quezon City, April 7, 1966.

ROMAN M. UMALI
Acting Presiding Judge

I CONCUR:

ESTANISLAO R. ALVAREZ
Associate Judge