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REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
MANILA

SALVADOR BOCANEGRA, JOAQUINA BOCANEGRA, IGNACIO BOCANEGRA, JOSEFA BOCANEGRA, ANA BOCANEGRA, MARIA TERESA LARRABASTER, MARIA ANTONIA LARRABASTER, JUAN LARRABASTER, FRANCISCA BOCANEGRA, CELESTINA BOCANEGRA, MARIA ANGELES BOCANEGRA, as Heirs of the Estate of the Deceased Dña. Manuela Montenegro Vda. de Bocanegra,
Petitioners,

October 12

- versus -

C.T.A. CASE NO. 420

COLLECTOR OF INTERNAL REVENUE,
Respondent.

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D E C I S I O N

The petitioners are seeking the refund of the sum of ₱10,975.45, the estate and inheritance taxes, plus penalties, assessed against and paid by them on the estate left by the deceased, Doña Manuela Montenegro Vda. de Bocanegra.

Doña Manuela Montenegro Vda. de Bocanegra died on August 27, 1946 leaving a will. Administration proceedings were instituted in the Court of First Instance of Negros Oriental for the settlement of the estate of the deceased. The will was admitted to probate and the appointment of the Compania General de Tabacos de Filipinas as executor of the will was approved. With the consent and approval of the probate court, the Compania General de Tabacos de Filipinas appointed and delegated Ramon F. de Altonaga as executor of the will and administrator of the estate.

On January 13, 1950, the administrator filed the corresponding estate and inheritance tax return for the estate of the deceased wherein it is shown that the claimed deductions exceed the value of the real and personal properties left by the deceased, to wit:

Real properties	₱122,700.00	
Personal properties	11,079.16	
Total value of estate		₱133,779.16
Deductions:		
Funeral expenses..	₱ 1,500.00	
Claims against estate	144,619.60	
Total deductions		₱146,119.60

On the basis of said return no estate or inheritance tax is due.

After due investigation, an examiner of the Bureau of Internal Revenue reported that the total fair market value of the estate on the date of death of the deceased was ₱286,663.06 and the total deductions allowable amount to ₱118,858.38, leaving a net estate in the amount of ₱167,804.68, which is subject to the estate and inheritance taxes and penalties in the sum of ₱10,975.46, itemized and computed as follows:

Gross estate:		
Real properties ------------		₱251,253.37
Personal properties ----------		35,409.69
Total ----------------------		₱286,663.06
Deductions:		
Funeral expenses-	₱ 1,500.00	
Judicial expenses-	3,768.88	
Claims against the estate -----	113,589.50	
Total ----------------------		₱118,858.38
Net estate -------------------		₱167,804.68
Estate tax -------------------		₱ 4,306.26
25% surcharge ---------------		1,076.57
Interest --------------------		1,873.22

Inheritance tax ------------------	2,194.27
25% surcharge ------------------	548.54
Interest ----------------------	951.59
Compromise:	
For failure to file notice of death ------------------------	5.00
For late filing of return ------	20.00
Total taxes and penalties -------	₱ 10,975.45

The liability of the estate for the payment of the sum of ₱10,975.45 was the result mainly of the increase in the valuation of the properties left by the deceased from ₱133,779.16 to ₱286,663.06 and the disallowance of the deduction of the sum of ₱31,284.38, representing part of the indebtedness of the deceased which was condoned by the creditors.

A demand was made by respondent against the administrator for the payment of the sum of ₱10,975.45, which was paid under protest on August 29, 1955. This action has been instituted by the heirs of the deceased for recovery of the said amount. Petitioners assail the correctness of the assessment, hence the legality of the collection of the sum of ₱10,975.45, solely on the grounds that the valuation placed by respondent on the estate is excessive and that the disallowance of the deduction of the condoned indebtedness is not in accordance with law. The two issues have been correctly and succinctly presented by counsel for petitioners, as follows:

> "There are only two simple issues in this case - one a question of fact and the other a question of law.
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> "The question of fact is with reference to the valuation of the estate for purposes of the estate and inheritance taxes. Which valuation is more in accord with the facts as they existed at the time of the death of Doña Manuela Montenegro Vda. de Bocanegra - the valuation of ₱133,779.17 made by the administrator or the valuation of ₱286,663.06 ar-

rived at by the examiner of the Bureau of Internal Revenue?

"The question of law arises from the undisputed fact that of the claims against the estate amounting to ₱144,619.60 as duly presented to and approved by the probate court in due course of administration, ₱31,284.38 were were condoned by the respective creditors after the death of the deceased. The question of law is whether such condoned indebtedness should be allowed as deductions from the gross estate." (Pp. 8-9, Memorandum for Petitioners, May 13, 1959.)

The first issue relates to the correctness of the determination made by respondent as to the fair market value of the real and personal properties left by the deceased. For estate and inheritance tax purposes, the estate is to be valued at its "fair market value".

"The estate shall be appraised at its fair market value as of the time of death, or as of six months thereafter, at the election of the executor or administrator in the case of the estate tax or the heirs in the case of inheritance tax. However, for the purpose of determining the value of real property, the assessed value as of the time of death, or, at the election of the executor, administrator or the heirs, as of six months after death, as shown by the tax rolls shall be considered as the fair market value, unless the contrary is shown." (Sec. 91, Revenue Code.)

The law requires that the estate be valued at its "fair market value" but contains no definition of the term. Neither does the law provide for the rules to be observed in determining "fair market value". However, the term has been judicially defined thus:

"The term 'market value' is not an absolute term; it involves human equation. Valuation is an inexact science and the value reached by whatever method must remain an approximation. A valuation of absolute accuracy is impossible. This impossibility of precise valuation is generally recognized;

the law is not so exact as to require mathematical certainty. Generally, however, the market value of property is the price which it will bring when it is offered for sale by one who desires, but is not obliged to sell it, and is bought by one who is under no necessity of having it." (II Formilleza, Commentaries and Jurisprudence on the National Internal Revenue Code, page 397, citing City of Manila v. Estrada, 25 Phil. 208; Manila Railway Co. v. Fabie, 17 Phil. 206; Manila Railroad Co. v. Alano, 36 Phil. 500; Manila Railroad Co. v. Velasquez, 32 Phil. 286; Manila Railroad Co. v. Caligsihan, 17 O.G. 1845; Lewis on Eminent Domain (2d), sec. 473; Stock Yards Case, 120 Mo. 541.)

The problems involved in valuation have been correctly stated by counsel for petitioner. We quote:

"Valuation is an old story in the tax law. Value is essentially and peculiarly a difficult question of fact. (Mary A. B. DuPont Land, 38 BTA 926, 928.) Market value 'is x x x dependent upon times, places, conditions and people. It is unsafe to neglect any apparent factor.'

"What criteria should be used in valuing real estate? 'Many factors must be considered, such as the location and condition of the property, the character and tendency of the neighborhood, pending improvements, adverse developments, suitability for special purposes, and so on.' (Paul, Federal Estate and Gift Taxation, Sec. 18.07, p. 1227, quoting from Reports to the Joint Committee on Internal Revenue Taxation, Federal and State Death Taxes, Vol. 2, pt. 2. p. 126.) The standard of value contemplated by the estate tax statute is the fair market value of property at the precise time of valuation, the time of death in our particular case, which 'fair market value' is commonly defined as the price at which the property would change hands between a willing buyer and a willing seller, neither under compulsion to buy or sell." (Memorandum for Petitioners, p. 9, May 13, 1959.)

With the foregoing statement of the law and the factors commonly used in the determination of the fair market value of property at a given time, we will now proceed to consider which of the two valuations, the one made by respondent or the one submitted by the administrator of the estate, approximates the fair market value as contemplated by law. We will first take up the valuation of the real properties.

In filing the estate and inheritance tax return the administrator valued the real properties at their assessed value. On the other hand, respondent valued the properties at rates higher than their assessed values following the information and advice received from the Provincial Assessor of the province where the properties are located. It is contended on behalf of petitioners that the valuation submitted by the administrator should be given more weight because said administrator, "in valuing the estate brought to bear personal knowledge and experience, not only personal knowledge of the property itself but experience in the appraisal of such kinds of properties." Considering, however, the presumption in favor of the correctness of determinations made by the Commissioner of Internal Revenue, the burden of proof is on petitioners to show not only that the determination made by the Commissioner in this case is wrong but also what is correct. Proving the incorrectness of the Commissioner's determination is not enought proof of the correctness of petitioners' position is also essential. Failure to establish both will result in the affirmance of the Commissioner's determination. Let us scrutinize the facts.

The first group of real properties is the Hacienda Tamogong which comprises the following parcels of land:

Description	Assessed Value
1. Tax Declaration No. 6492 (Lots Nos. 802, 803, 804, 805, 807, 808, 809, 810, 811, 813, 818, 373, 378) ---------	₱ 76,790.00
2. Tax Declaration No. 6161 (Lot No. 247) ---------------	7,310.00
3. Tax Declaration No. 6162 (Lot No. 360) ---------------	6,230.00
4. Tax Declaration No. 6713 (Lot No. 376) ---------------	1,560.00
5. Tax Declaration No. 6711 (Lot No. 377) ---------------	1,950.00
Total ------------	₱ 93,840.00

The administrator claims that the sum of ₱93,840.00 (not ₱93,480.00 as shown in Exh. C), which is the total assessed value of the various parcels of land comprising the Hacienda Tamogong, represents the fair market value thereof at the time of death of the deceased in 1946. It is alleged that the hacienda was "in a state of abandonment due to the recent war. It was full of outgrowth, small trees. It was practically unfit for cultivation." He admits, however, that in August, 1946, "a very small portion of it they tried to be cleaned and planted."

An examination of the records shows that the lots covered by Tax Declaration No. 6492 (Exh. E) were assessed for real property tax purposes in 1939; the lot covered by Tax Declaration No. 6161 (Exh. F) in 1937; the lot covered by Tax Declaration No. 6162 (Exh. G) in 1937; the lot covered by Tax Declaration No. 6713 (Exh. H) in 1940; and the lot covered by Tax Declaration No. 6711 (Exh. I) in 1940. It is an undisputed fact that the assessed value of real property for real property tax purposes does not represent its fair market value even at the time the assessment is made. The assessed value is always less than the fair market value.

Real property taxation was recently the subject of an extensive study and survey by two officials of the FOA (now ICA) Mission in the Philippines, with the assistance of provincial and city assessors and other officials connected with real property taxation. In their report to the Secretary of Finance dated November 6, 1953, they made the following conclusions:

> "(a) Assessed values of all categories of land studied in this report are substantially below market values of such land. Average ratios of assessed to market values are 65 per cent for commercial land in chartered cities and 54 per cent in provinces, 66 per cent for residential land in chartered cities and 50 per cent in provinces, and 62 per cent for farm land in cities and 51 per cent in provinces. Thus the apparently better trained personnel, the smaller area to be covered and the preponderance of commercial land in the cities makes for a more efficient and up-to-date assessment pattern.
>
> "(b) Variations for different cities and provinces of the ratio of assessed to market values are very pronounced. Such variations apply to all types of land and the ratios in question are as low as 13 per cent to 10 per cent in several cities and provinces and as high as 90 per cent to 100 per cent in others. This would indicate that to adjust the tax rates without revising the assessments would probably only compound the disparities existing in the present structure. It is believed that the ratios of assessed to market value reported by local officials and employed in this study represent, in most cases, estimates by those officials rather than the results of actual surveys and are biased upward. The independent surveys referred to in this study tend to support this opinion.
>
> "(c) The schedule of valuations used for assessment purposes are applied with unwarrant-

ed rigidity and are generally far out of date insofar as they purport to provide a satisfactory basis for assessing farm land for tax purposes. The lack of uniformity of the ratios of assessed to market value indicates that that the Provincial and Municipal Finance Division of the Department of Finance has failed to coordinate the valuation schedules used in different provinces, perhaps because of insufficient data to determine reasonable market value of properties throughout the Philippines. Increases in valuation schedules since 1946 only very partially reflected increases in real property values and for the most part the schedules are based on 1941 or earlier valuations.

"(d) As noted above, there is a clear indication that the assessed value of urban land bears a higher ratio to market value than land in the provinces and that the ratio of assessed to market value for commercial land is higher than for farm land. Residential land falls between the other two types of land. However, for the same general category (i.e., farm land) in the same area there seems to be considerable uniformity as to the ratios of assessed to market value for different types (rice land, corn land, sugar land, etc.). Unit assessed values of farm land tend to decrease somewhat with the size of the parcel but this may be explained by the fact that better quality land may be cultivated in small parcels. Provinces differ greatly in this respect, however, and in several instances the change in average unit value for different sized parcels is so striking as to raise strong doubts as to the accuracy of the application of valuation schedules. (See Table 3)" (Taxation of Real Property in the Philippines, Analysis and Recommendations, by Melville A. Monk, Chief Finance and Tax Advisor, and O. J. McDiarmid, Assistant Director for Economic Policy, FOA Mission.)

Surely, the assessments made in 1937, 1939 and 1940 cannot be accepted as the fair market values of the properties in 1946, even without considering the fact that the value of real property tends to increase with the passing of the years.

But it is contended that the hacienda was in a state of abandonment due to the recent war; that it was full of outgrowth; and that it was practically unfit for cultivation, although a very small portion was tried to be cleaned and planted. How much of the hacienda was tried to be cleaned and planted? No evidence has been adduced to show the extent or area which was cleaned and planted. It appears, however, from the project of partition (Exh. A) that on the date of death of the deceased there was a standing crop which was valued by the administrator at ₱8,571.14. The examiner of the Bureau of Internal Revenue valued the standing crop at ₱10,812.40, which is the total of the expenses incurred in production. (See Exh. 3-C, page 23, BIR records.) The correctness of the findings of the internal revenue examiner has not been disputed. If a portion of the hacienda was cultivated and planted, and the sum of ₱10,812.40 was actually spent to produce a standing crop, it is obvious that the area cultivated and planted could not have been a "very small portion". If petitioners wanted a more accurate valuation of the estate, they should have proved the actual area under cultivation and the area of the uncultivated portion, and the fair market value of each portion.

Also, the allegation that the hacienda was unfit for cultivation is not borne out by the evidence. It appears that during the period of administration of the estate, the administrator gave advances to the heirs in the total amount of ₱78,379.82 and paid a considerable portion of the indebtedness of the deceased. The total indebtedness left by the deceased was ₱144,619.60, of which only ₱48,104.25 remained unpaid when the project of partition was submitted to the probate court. Obviously, the advances to the heirs and the amounts paid to the creditors were merely a part of the earnings of the estate, attesting to its productivity.

The foregoing circumstances have impelled us to reject the proposition that the assessed values of the various parcels of land comprising the Hacienda Tamogong in 1937, 1939 and 1940 represent the fair market values thereof in 1946.

The same is true with respect to the other parcels of land. Most of these lands were assessed for real property tax purposes in 1939, 1940 and 1941, and one parcel of land (Tax Declaration No. 6549, Exh. P) was assessed as far back as 1927.

The center of attack against the correctness of the appraisal made by respondent is the valuation of sugar lands at ₱1,500.00 per hectare. But not all the sugar lands were appraised by respondent at ₱1,500.00; some were valued at ₱1,200.00 per hectare. The internal revenue examiner submitted an itemized statement of all the properties of the deceased. (See Exhs. 3 to 3-D, pp. 22-26, BIR records.) From this statement, it appears that the sugar lands in the Hacienda Tamogong have been appraised at ₱1,500.00 per hectare; other sugar lands at ₱1,200.00 and ₱1,500.00 per hectare; corn lands at ₱300.00 and ₱500.00 per hectare; rice land at ₱400.00 per hectare; coconut lands at ₱300.00 and ₱500.00 per hectare; and abaca lands at ₱500.00 per hectare. That the examiner did not actually see these lands is not evidence of the incorrectness of his appraisal, there being sufficient evidence of its reasonableness, and petitioners themselves not having established the correctness of their own appraisal.

As regards the personal properties, the following is a comparative statement of the valuation made by respondent and the administrator:

Description	Valuation Made by Administrator[1]	Valuation Made by Respondent[2]
1. Utiles y aperos d de labranza ----	₱4,025.00	₱4,025.00
2. Material de via portatil--------	2,670.00	4,735.00
3. Vehiculos --------	119.00	120.00
4. Ganado de labòr --	360.00	600.00
5. Accesorios y herramientas varies -	259.00	306.00
6. Mobiliario y ajuar	1,234.00	2,480.00
7. Caja ------------	28.79	28.79

From the evidence, we find that the valuation made by respondent is neither excessive nor unreasonable. Only items 2, 4 and 6 were substantially increased. In the case of item 3, the sum of ₱119.00, the valuation made by the administrator, was raised merely to ₱120.00 "to round the figures". This has been assailed as arbitrary and unreasonable. We quote from the memorandum of counsel for petitioners:

> "While the increase is insignificant, amounting in this instance to only a few pesos, it is significantly indicative of the arbitrary and rather unreasonable manner in which the valuations placed by the adminis-

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[1]Exhibits C to C-3, pp. 51-55, C.T.A. records.

[2] Exhibit 3-A, p. 25, BIR records.

> trator were increased in order to justify the imposition of estate and inheritance taxes. It is respectfully submitted that while it is an admitted proposition that the government revenue must be protected, the government should not play the ignoble role of assessing arbitrary impositions." (Memorandum for Petitioners, May 13, 1959, p. 33.)

If rounding of figures is arbitrary and unreasonable, petitioners are equally guilty of the same error. To cite a few examples: In Tax Declaration No. 6492 (Exh. E), the properties described therein were appraised at ₱76,792.53, yet the amount taken into account as the assessed value is ₱76,790.00. In Tax Declaration No. 6162 (Exh. G), the property was appraised at ₱6,234.00, yet the amount considered as the assessed value is ₱6,230.00. And in Tax Declaration No. 6713 (Exh. H), the property was appraised at ₱1,562.75, but the amount was reduced to ₱1,560.00.

The last item involving the question of valuation is the leasehold rights possessed by the deceased over Hacienda Sto. Niño by virtue of a five-year contract of lease entered into by the deceased with one Marcelo Retes. Respondent claims that the value of the leasehold is ₱12,312.50, computed on the basis of ₱1.00 per picul of sugar quota per year for the life of the lease, which was to run for five years. Petitioners admit that "the leasehold right might have had some value", but it is alleged that there is no evidence "that such right had a market value."

If property, or property right, has some value, it cannot escape taxation merely because the taxpayer claims it has no market value. If the taxpayer has made no attempt to assess its value, it is the duty of the Commissioner of Internal Revenue to determine its value by any method which may be considered fair and reasonable. In the instant case, respondent determined the value of the leasehold right on the basis of ₱1.00 per picul of sugar quota assigned to the hacienda leased. Petitioners claim it is arbitrary without showing why, and they have made no attempt to prove its actual or approximate value. In the absence of a more reasonable basis than the one adopted by respondent, his determination has to be sustained.

The second issue refers to the deductibility from the gross estate of a part of the indebtedness of the deceased which was condoned by the creditors. Of the total indebtedness in the amount of ₱144,619.60, the sum of ₱31,284.38 was condoned by the creditors. The deduction from the gross estate of the sum of ₱31,284.38 was disallowed by respondent.

The law allows the deduction from the gross estate, to arrive at the taxable net estate, of claims against the estate. The deductibility of claims against the estate is "limited to the extent that they were contracted *bona fide* and for an adequate and full consideration in money or money's worth." (Section 89, Revenue Code.) Petitioners contend that the sum of ₱31,284.38 was an indebtedness contracted *bona fide* and for an adequate and full consideration in money or money's worth, and therefore deductible. We agree with respondent that it is not deductible. The "claims against the estate" which the law allows as deduction from the gross estate are <u>existing</u> claims against the estate. An indebtedness that has been condoned is in legal effect no indebtedness at all. If there is no more indebtedness by reason of the condonation, there is no claim against the estate which may be allowed as deduction. Whether or not the condonation resulted in a taxable gift need not here be decided.

Certain authorities have been cited by counsel for petitioners allegedly permitting the deduction of such claims "regardless of the collectibility of such claims or whether or not such claims are later paid by the estate." The authorities cited are not in point. None of the cases referred to involved condoned indebtedness. All of them involved subsisting indebtedness or claims against the estate which could not be satisfied because of the insufficiency of the assets or of the insolvency of the estate. There is a wide gap that separates condoned indebtedness from indebtedness that cannot be satisfied by reason of the insufficiency of funds or of the insolvency of the debtor.

FOR THE FOREGOING CONSIDERATIONS, the claim for refund is hereby denied. With costs against petitioners.

SO ORDERED.

Manila, October 12, 1959.

ROMAN M. UMALI
Associate Judge

WE CONCUR:

MARIANO NABLE
Presiding Judge

AUGUSTO M. LUCIANO
Associate Judge