MARIANO ZAMORA,
Petitioner,

- versus -

C.T.A. CASE NO. 234

December 29, 1958

COLLECTOR OF INTERNAL REVENUE,
Respondent.

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D E C I S I O N

This is an appeal from the decision of the respondent requiring the petitioner to pay the sums of ₱43,758.00 and ₱7,625.00 as deficiency income tax for the years 1951 and 1952, respectively. The said sums have been arrived at as follows:

1951

Net income as per return ----------------		₱ 29,935.18
Add: A. Deductions disallowed:		
1. General & miscellaneous expenses:		
(a) Matriculation & School fees (not contested)	₱1,392.20	
(b) Contribution to political parties	10,000.00	
(c) Christmas gifts (not contested)	648.10	
(d) Funeral expenses (not contested)	150.00	
(e) Food & coffee (not contested)	32.70	
(f) Arrow shirts (not contested)	50.00	
(g) Hotel & representation expenses of Mr. M. Zamora abroad in 1951 (considered capital expenditures)	13,513.22	
(h) Traveling expenses of Mr. H. Aguinaldo who was taken by M. Zamora to U.S. in 1951 (considered capital expenditure)	1,562.40	₱27,348.62
2. Promotion expenses of Bay View Hotel (½ allowed) ----------------		10,478.50
3. Taxes - Penalty & Special assessment (not questioned) ------------		94.14
4. Overcharged depreciation of the Bay View Hotel:		

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Depreciation claimed for 7 months at 3½% a year ...	₱28,249.97	
Less: Depreciation allowed for 7 months at 2½% a year	20,188.55	8,061.42
B. Income not declared:		
1. Pre-war accounts payable written off-- and credited to Capital account		2,933.44
2. Fifty percent (50%) of long term capital gain realized from the sale of lots		49,540.50
T o t a l -------------------------------		₱128,391.80
Less: Deduction allowed: Depreciation for 7 months on capital expenditures which were disallowed as deduction during the year 1951 (10% of ₱15,075.62 multiplied by 7/12) -----------------------		879.41
Net income as per adjustment ------------		₱127,512(.39)
Less: Personal and additional exemptions--		5,400.00
Net income subject to tax ---------------		₱122,112.00
Tax due thereon -------------------------		₱ 48,739.00
Less amount paid (O.R. Nos. 31126 & 383573) -------------------------		4,981.00
DEFICIENCY TAX DUE AND COLLECTIBLE -------		₱ 43,758.00

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Net income as per return ----------------		₱ 21,369.26
Add: A. Deductions disallowed:		
1. Expenses re intestate proceedings of F. Zamora charged to Legal & Auditing Fees (not contested) -------------------		433.70
2. Surcharge on sales tax & compromise charged as taxes (not contested)----		354.08
3. Representation & entertainment expenses considered as personal expenses (1/3 of ₱3,770.00 after deducting ₱225.00 as additional salary of Mr. Teodoro Uy) ---------		1,181.67
4. Traveling & transportation expenses of Mr. Zamora to the United States:		
(a) Amount not supported ..₱	134.00	
(b) Amount considered spent for personal purposes (medical treatment)............₱	3,511.30	₱ 3,645.30
5. Christmas gifts not supported (Admitted) ----------------------		1,017.80
6. Miscellaneous & gene ral expenses personal (board & lodging of Auring at St. Joseph College) (Admitted) ---		615.50
7. Bad debt written off (Nick Osmeña, considered solvent) (Not contested)--		2,548.37
8. Depreciation claimed on Bay View Hotel Building for 4 months only(Jan.-April) ....₱16,142.85		

Less: Depreciation allowed (25% of ₱1,383,673.24 multiplied by 4/12) -------	₱11,527.94	₱4,614.91

B. Income not declared:

1. Fifty percent (50%) of long term capital gain derived from the sale of land -------------------------------	10,267.63
T o t a l ---------------------------------	₱46,048.22
Less: Deduction allowed: Depreciation for 4 months on capital expenditures which were disallowed as deduction during the year 1951 (10% of ₱15,075.62 multiplied by 4/12) ----------------------------	502.52
NET income as per adjustment ------------	₱45,545.(70)
Less: Personal and additional exemptions--	5,400.00
Net income subject to tax --------------	₱40,145.00
Tax due thereon -----------------------	₱10,278.00
Less: Amount paid 5/14/53 O.R. No. 434329 & 8/14/53, O.R. No. 444423)	2,653.00
DEFICIENCY TAX DUE AND COLLECTIBLE -------	₱ 7,625.00

This case was heard jointly with C.T.A. No. 194 (Esperanza A. Zamora, in her capacity as Special Administratrix of the estate of the deceased Felicidad Zamora v. Collector of Internal Revenue), the sole issue in that case being one of the issues raised in this case.

Petitioner Mariano Zamora is the owner of Bay View Hotel and Farmacia Zamora. He filed his income tax returns for the years 1951 and 1952. After investigation and examination of said returns, respondent found that petitioner failed to declare his income derived from the sale of certain real properties and claimed deductions which are not allowable. Hence, the deficiency assessment mentioned above.

Petitioner admits the correctness of the decision of respondent with respect to the disallowance of the deductions claimed in his income tax returns for 1951 and 1952 and the alleged underdeclaration of certain incomes, except as regards the following items:

1. Deductions disallowed:
   a. Promotion expenses of Farmacia Zamora and Bay View Hotel, 1/2 of ₱20,957.00 -------- ₱10,478.50
   b. Overcharged depreciation
      (1) 1951 ------------- 8,061.42
      (2) 1952 ------------- 4,614.91

2. Undeclared income:
   a. 1951- 50% of capital gain derived from the sale of real property in Malate, Manila, and Quezon City 49,540.50
   b. 1952- 50% of capital gain derived from the sale of another real property in Quezon City--- 10,267.63

The sole issue, therefore, relates to the correctness of the deficiency income tax assessment as affected by the disputed items mentioned above.

The sum of ₱20,957.00 was deducted by petitioner from his income tax return for the year 1951. It is alleged that the said amount was spent by Mrs. Esperanza A. Zamora, wife of petitioner, during her travel to Japan and the United States to purchase machinery for a new "Tiki-tiki" plant and to observe hotel management and modern hotel trends. It appears, however, that for said trip Mrs. Zamora obtained only the sum of $5,000.00 from the Central Bank, and that in her application for dollar allocation she stated that she was going abroad on a combined medical and business trip. These facts are not denied by petitioner. And no evidence has been submitted where Mrs. Zamora obtained the amount in excess of the $5,000.00 given to her which she spent abroad. Neither has any explanation been made to show that the statement contained in Mrs. Zamora's application for dollar allocation that she was going abroad on a combined medical and business trip was not correct. In these circumstances, and in view of the fact that the alleged expenses are not supported by receipts, we believe respondent acted properly in disallowing one-half of the alleged expenses. (See Visayan Cebu Terminal Co., Inc. v. Collector of Internal Revenue, C.T.A. No. 128, June 29, 1957, citing Cohan v. Commissioner, 39 F (2d) 540, 8 AFTR 10552.)

For the years 1951 and 1952, petitioner claimed a deduction for depreciation of the Bay View Hotel building at the rate of 3-1/2% of the value of said building, pursuant to Section 30(f) of the Revenue Code. On the other hand, respondent believes that petitioner is entitled to a depreciation allowance of only 2-1/2%, and has accordingly disallowed the sums of ₱8,061.42 for 1951 and ₱4,614.91 for 1952. In allowing petitioner a depreciation deduction of 2-1/2% for the Bay View Hotel, respondent relied upon Bulletin "F" published by the Internal Revenue Service of the United States. Bulletin "F" contains a list of depreciable assets, the estimated average useful lives thereof and the rates of depreciation allowable for each kind of property. (See 1955 PH Federal Taxes, Pars. 14,160 to Par. 14,163-C.) It is true that Bulletin "F" has no binding force, but it has strong persuasive force considering that the same has been the result of scientific studies and observation for a long period in the United States after whose Income Tax Law ours is patterned.

Counsel for petitioner contends that the "functional life" of the Bay View Hotel building, or its normal useful life as a hotel building, must be considered in determining the rate of depreciation applicable there-and in view of the fact that the alleged expenses are not supported by receipts, we believe respondent acted properly in disallowing one-half of the alleged expenses. (See Visayan Cebu Terminal Co., Inc. v. Collector of Internal Revenue, C.T.A. No. 128, June 29, 1957, citing Cohan v. Commissioner, 39 F (2d) 540, 8 AFTR 10552.)

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Counsel for petitioner contends that the "functional life" of the Bay View Hotel building, or its normal useful life as a hotel building, must be considered in determining the rate of depreciation applicable there-to. The following special circumstances allegedly justify a depreciation rate of 3-1/2%:

> "As pointed out above, we are not concerned with how long the Bay View Hotel building will last physically. Rather, we must deal with its functional life, its normal useful life. We must consider how long it can, as a hotel, endure the 'tastes of a fickle public', how long the building will continue to function as a producing unit. On this point, petitioner's evidence to the effect that in '30 or 23 years the Bay View Hotel building will be considered worthless and will have to undergo a complete remodelling from top to bottom' (t.s.n., p. 108) has not been contradicted. On the contrary, this estimate of the 'normal useful life' of the building in question is borne out by these facts, namely: (1) The present trend in Manila is for office buildings to be constructed in the Ermita district, where precisely the Bay View Hotel building is located (t.s.n., p. 107). This would shorten the functional life of the latter because guests, who patronize first class hotels, prefer to stay in a quiet environment, away from the bustle of commercial activity (t.s.n., p. 127). (2) The Bay View Hotel has no room for expansion or improvement. It has no space for a swimming pool, a tennis court or even a night club. These are the usual attractions demanded by hotel guests. For lack of such recreational facilities, and the physical limitations precluding their introduction, the Bay View Hotel is no longer the first class hotel that it used to be a couple of years ago (t.s.n., pp. 122-124). One does not have to have foresight to foretell that in 20 years from now the Bay View Hotel building's functional worth would have been reduced to nil. (3) Foreign companies, such as the Pan-American Airways and the Hilton International Hotels, are planning to put up modern hotels in Manila (t.s.n., p. 110). This would make the Bay View Hotel, with its limited facilities, a collector's item. Take the Manila Hotel, for an example. Even without competition, the petitioner, as lessee thereof, had to spend ₱2,000,000.00 for improvements to make it presentable and a profit-earning hotel building (t.s.n., p. 108). It is of common knowledge that architectural changes and designs are playing a highly important role in the economic value and life of edifices. This will surely continue, if not aggravate, with the years, and is exceptionally true with respect to the hostelry business.

> In other words, changing modes in architecture, styles of furniture, and decorative designs - all these must meet the tastes of a fickle public (t.s.n., pp. 106-107)." (Pp. 9-11, Memorandum for Petitioner.)

Among the special circumstances mentioned as justifying a depreciation deduction of 3-1/2% are (1) the trend of Ermita district, where the Bay View Hotel is located, to become a commercial district; (2) the fact that the hotel has no room for improvement; and (3) the changing modes in architecture, styles of furniture, and decorative designs, all of which must meet the tastes of a fickle public. We find, however, that in estimating the reasonable rate of depreciation allowance for hotels made of concrete and steel at 2-1/2%, the factors mentioned by counsel have been taken into account. Normally, an average hotel building is estimated to have a useful life of 50 years, but inasmuch as the useful life of the building for business purposes "depends to a large extent on the suitability of the structure to its use and location, its architectural quality, the rate of change in population, the shifting of land values, as well as the extent of maintenance and rehabilitation," it is allowed a depreciation rate of 2-1/2% corresponding to a normal useful life of only 40 years. (1955 PH Federal Taxes, Par. 14,160-K.) Consequently, the stand of petitioner cannot be sustained.

The possibility that foreign companies, such as the Pan-American Airways and the Hilton International Hotels, may put up modern hotels in Manila, in which event the Bay View Hotel would be merely "a collector's item", is a matter that apparently involves deduction for extraordinary obsolescence, not an ordinary depreciation deduction. (See Sec. 110, Rev. Regs. No. 2; 1955 PH Fed. Taxes, Pars. 14,175, 14,177.)

We are, therefore, of the opinion that the rate of 2-1/2% determined by respondent as a reasonable allowance for depreciation of the Bay View Hotel is in order.

The next item in dispute is the sum of ₱49,540.00, representing 50% of the undeclared capital gain derived from the sale in 1951 of certain real properties in Malate, Manila, and in Quezon City, all of which were acquired during the Japanese occupation. It appears that the Manila property was acquired on May 16, 1944 for ₱132,000.00 and sold on March 5, 1951 for ₱75,000.00. This property was owned jointly by petitioner and his sister, the late Felicidad Zamora. The Quezon City property was acquired on January 19, 1944 for ₱68,000.00 and sold on February 9, 1951 for ₱94,000.00.

We have already held in the case of Esperanza Zamora v. Collector of Internal Revenue, C.T.A. No. 194, December 29, 1958, that the cost basis of property acquired in Japanese war notes is the equivalent of the war notes in genuine Philippine currency in accordance with the Ballantyne Scale of values, and that the determination of the gain derived or loss sustained in the sale of such property is not affected by the decline at the time of sale in the purchasing power of the Philippine currency. We quote from the decision in said case:

> "On the assumption that the purchase price of ₱132,000.00 was entirely paid in

Japanese war notes, the cost of the property cannot be ₱132,000.00 in genuine Philippine currency. It is an admitted fact that during certain periods of the enemy occupation, the value of the Japanese war notes was very much less than the value of the genuine Philippine currency. It is for this reason that the Ballantyne Scale of values, which was the result of an 'impartial scientific study', has been adopted and given judicial recognition. (Garrido v. North Camarines Lumber Co., 44 O.G. 4401; Berlongan v. Pascual, 45 O.G. 222.) If the value of the Japanese war notes in May, 1944, when the property was bought, was one-twelfth of the genuine Philippine peso, and since the gain derived or loss sustained in the disposition of said property is to be reckoned in terms of Philippine peso, the value of the Japanese war notes used in the purchase of the property must be reduced in terms of the genuine Philippine peso to determine the cost of acquisition.

"It is, however, contended that if the purchase price in Japanese war notes is to be converted into the pre-war value of the Philippine peso, the selling price of the property in 1951 should also be reduced to its pre-war value, it being admitted that the value of the peso in 1951 was much lower than its pre-war value. This appeared to us at first as a valid argument, and for this reason the case was reopened to enable the parties to submit evidence of the value of the peso in 1951 as compared to its pre-war value. The parties, however, failed to establish definitely the value of the peso in 1951 as compared to its pre-war value. At any rate, after a more thorough study of the question, we have arrived at the conclusion that there is no legal basis for considering the rise and fall of the value of the currency in determining the gain derived or loss sustained in the sale or disposition of property. (See Gutierrez v. Collector of Internal Revenue, C.T.A. No. 65, Aug. 31, 1955, affd. in G. R. Nos. L-9738 & L-9771, May 31, 1957.)"

It is alleged, however, that, in the case of the Manila property which was acquired for ₱132,000.00, one-half of the purchase price, or ₱66,000.00, was paid in Philippine currency, while the other half was paid in Japanese war notes. After a careful consideration of the evidence, we found that the claim that ₱66,000.00 was paid in Philippine currency has been sufficiently established. For this reason, the capital gain derived from the sale of said property is ₱3,500.00, instead of ₱64,000.00 as previously determined by respondent. The property being jointly owned by petitioner and his sister, the late Felicidad Zamora, the share of petitioner in the profit realized from the sale of the property is ₱1,750.00. Again, to quote from the decision in Esperanza Zamora v. Collector of Internal Revenue, supra:

> "Finally, it is alleged that the purchase price of ₱132,000.00 was not entirely paid in Japanese war notes. Mariano Zamora, co-owner of the property in question, testified that ₱66,000.00 was paid in Philippine currency and the other ₱66,000.00 was paid in Japanese war notes. No evidence was presented by respondent to rebut the testimony of Mariano Zamora; it is assailed merely as being improbable. We have examined this question thoroughly and we are inclined to give credence to the allegation that a portion of the purchase price of the property was paid in Philippine money. In the first place, it appears that the Zamoras owned the Farmacia Zamora which continued to engage in business during the war years and that a considerable portion of its sales was paid for in genuine Philippine currency. This circumstance enabled the Zamoras to accumulate Philippine money which they used in acquiring the property in question and another property in Quezon City. In the second place, ₱132,000.00 in Japanese war notes in May, 1944 is equivalent to only ₱11,000.00. The property in question had at the time an assessed value of ₱27,031.00 (in Philippine currency). Considering the well known fact that the assessed value of real property is very much below its fair market value, it is incredible that said property should have been sold by the owner thereof for less than one-half of its assessed value. These facts have convinced us of the veracity of the allegation that of the purchase price of ₱132,000.00 the sum of ₱66,000.00 was paid in Philippine currency, so that only the sum of ₱66,000.00 was paid in Japanese war notes.

> "Since the sum of ₱66,000.00 in Japanese war notes in May, 1944 is equivalent to ₱5,500.00 in Philippine currency (₱66,000.00 divided by 12), the acquisition cost of the property in question is ₱66,000.00 plus ₱5,500.00, or ₱71,500.00. The property was sold for ₱75,000.00 in 1951, so that the owners thereof, Mariano and Felicidad Zamora, derived a capital gain of ₱3,500.00, or ₱1,750.00 each. x x x ."

In the case of the Quezon City property, it is alleged that the entire purchase price of ₱68,959.00 was paid in Philippine currency. As in the case of the Manila property, we are inclined to believe the allegation of petitioner. If, as contended by respondent, the purchase price of ₱68,959.00 was paid in Japanese war notes, the purchase price in Philippine currency would be only ₱17,239.75 (₱68,959.00 divided by 4, ₱4.00 in war notes being equivalent to ₱1.00 in Philippine currency). The assessed value of said property in Philippine currency at the time of acquisition was ₱46,910.00. It is quite incredible that real property with an assessed value of ₱46,910.00 should have been sold by the owner thereof in Japanese war notes with an equivalent value in Philippine currency of only ₱17,239.75. We are more inclined to believe the allegation that it was purchased for ₱68,959.00 in genuine Philippine currency. Since the property was sold for ₱94,000.00 on February 9, 1951, the gain derived from the sale is ₱15,361.75, after deducting from the selling price the cost of acquisition in the sum of ₱68,959.00 and the expenses of sale in the sum of ₱9,679.25. (See page 13, Memorandum for Respondent.)

Accordingly, the total undeclared income of petitioner derived from the sales of the Manila and Quezon

City properties in 1951 is ₱17,111.75 (₱1,750.00 plus ₱15,361.75), 50% of which in the sum of ₱8,555.88 is taxable, the said properties being capital assets held for more than one year. (See Section 34(b), Revenue Code.)

The last item in dispute is the sum of ₱10,267.63, representing 50% of the capital gain derived from the sale in 1952 of another real property in Quezon City. Petitioner claims that 50% of the capital gain derived from the sale is only ₱9,320.52. Respondent has agreed to the correctness of the said amount. (Page 18, Memorandum for Respondent.)

In view of the foregoing, the deficiency income tax due from petitioner for 1951 is ₱22,980.00, and for 1952, ₱7,278.00, computed as follows:

1951

Net income per respondent --------	₱127,512.39
Less: Difference between ₱49,540.50 (50% of capital gain from sale of real property in 1951 as found by respondent) and ₱8,555.88 (50% of capital gain from sale of same property as found by this Court) --------	40,984.62
Adjusted net income ---------------	₱ 86,527.77
Less: Personal exemptions ----------	5,400.00
Net Taxable income ----------------	₱ 81,127.77
Tax due on ₱81,127.77 -------------	₱ 27,961.00
Less: Amount previously paid -------	4,981.00
Deficiency tax --------------------	₱ 22,980.00

1952

Net income per respondent ----------	₱ 45,545.70
Less: Difference between ₱10,267.63 and ₱9,320.52 ---------------	947.11
Adjusted net income ---------------	₱ 44,598.59
Less: Personal exemption -----------	5,400.00
Net taxable income ----------------	₱ 39,198.59
Tax due on ₱39,198.59 -------------	₱ 9,931.00
Less: Amount previously paid -------	2,653.00
Deficiency tax --------------------	₱ 7,278.00

SUMMARY

1951 deficiency income tax--	₱22,980.00
1952 deficiency income tax--	7,278.00
Total deficiency income tax -------------------	₱30,258.00

WHEREFORE, the decision appealed from is hereby modified, and petitioner is hereby ordered to pay the sum of ₱30,258.00 as deficiency income tax for the years 1951 and 1952, within thirty (30) days from the date this decision becomes final, plus the corresponding surcharge and interest in case of delinquency, pursuant to Section 51(e) of the Revenue Code. With costs against petitioner.

SO ORDERED.

Manila, December 29, 1958.

ROMAN M. UMALI
Associate Judge

WE CONCUR:

MARIANO NABLE
Presiding Judge

AUGUSTO M. LUCIANO
Associate Judge

Aff'd. G.R. L-15290 + 15280, May 31, 1963.