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REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
MANILA

ANTONIO PORTA FERRER,
Petitioner,

- versus -

C.T.A. CASE NO. 503

COLLECTOR OF INTERNAL REVENUE,
Respondent.

August 27, 1959

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D E C I S I O N

This is an action for the refund of the amount of ₱2,030.00 claimed to have been erroneously paid by petitioner as excess income tax for the year 1955.

Petitioner, Antonio Porta Ferrer, was the sole proprietor of the "La Suiza Bakery" located at 1002 R. Hidalgo, Quiapo, Manila from October 16, 1951 up to September 15, 1955 when said bakery was sold to one Jose Pons (Exh. 4, pp. 44-45, BIR rec.) for the sum of ₱100,000.00 (Exh. A, pp. 35-36, CTA rec.). The assets of the business consisted of accounts receivable, raw materials, wrapping supplies, firewood, unexpired insurance, goodwill, machinery and equipment, delivery equipment, and furniture and fixtures having a total book value of ₱74,321.91. This value is itemized as follows:

	COST	DEPRE-CIATION	BOOK VALUE
Accounts Receivable	₱13,523.29		₱13,523.29
Raw Materials	16,205.35		16,205.35
Wrapping Supplies	3,387.58		3,387.58
Firewood	68.20		68.20

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Unexpired Insurance	₱ 1,049.01		₱ 1,049.01
Goodwill	10,000.00		10,000.00
Machinery & Equipment	22,970.00	₱ 8,800.84	14,169.16
Delivery Equipment	27,214.56	14,590.94	12,623.62
Furniture & Fixtures	5,321.05	2,025.35	3,295.70
	₱99,739.04	₱25,417.13	₱74,321.91

(Exh. 2-E, p. 3, BIR rec.)

In the sale, he incurred expenses in the respective amounts of ₱5,000.00, broker's commission, and ₱1,000.00, accountant's fee, or a total of ₱6,000.00 (Exh. 2-E).

On February 14, 1956, petitioner filed his income tax return, which showed the sum of ₱19,678.09, as the net profit realized from the sale of the bakery (Exh. 1, pp. 1-2, BIR rec.).

On February 15, 1956, he paid ₱2,439.00 as income tax on the net profit realized from the sale transaction (Exh. C, p. 37, CTA rec.).

On the theory that the profit derived therefrom was a long term capital gain, and therefore was taxable only to the extent of 50%, petitioner, on February 4, 1958, requested for the refund of ₱2,030.00 (Exh. D, p. 39, BIR rec.). The request for refund has not been acted upon by respondent.

Hence, the instant appeal, which was instituted on February 15, 1958.

Subsequent to the filing of the petition for refund, respondent moved for the dismissal of the same on the ground that, there being no decision or ruling upon which the appeal can be premised, petitioner has no cause of action. This Court, in a majority opinion, applying the rationale in College of Oral and Dental Surgery vs. Collector, C.T.A.

Case No. 121, December 19, 1955; Paracale-Gumaus Consolidated Mining Co. vs. Collector, C.T.A. Case No. 211, August 22, 1956; Hume Pipe Asbestos Co., Inc. vs. Collector, C.T.A. Case No. 306, October 22, 1956; and Philippine Iron Mines, Inc. vs. Collector, C.T.A. Case No. 294, November 9, 1956, held that in a claim for refund, the taxpayer, after waiting within a reasonable time for the decision of the Commissioner, may institute the action without waiting for such decision so as not to be barred by the two-year period. Consequently, the motion to dismiss was denied.

The only remaining issue to be resolved is whether or not the sale by petitioner Antonio Porta Ferrer of the "La Suiza Bakery" constituted a sale of capital asset.

The law involved in this case is found in paragraphs (a) and (b) of Section 34 of the National Internal Revenue Code, the pertinent provisions of which are:

> "SEC. 34. Capital gains and losses.—
> (a) Definitions.— As used in this Title—
> (1) Capital assets.—The term 'capital assets' means property held by the taxpayer (whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, or property, used in the trade or business, of a character which is subject to the allowance for depreciation provided in subsection (f) of section thirty; or real property used in the trade or business of the taxpayer.
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> x x x x

> (b) Percentage taken into account.— In the case of a taxpayer, other than a corporation, only the following percentages of the gain or loss recognized upon the sale or exchange of a capital asset shall be taken into account in computing net capital gain, net capital loss, and net income:
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> (1) One hundred per centum if the capital asset has been held for not more than twelve months;
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> (2) Fifty per centum if the capital asset has been held for more than twelve months."

Petitioner contends that what was actually sold by him was the entire bakery business which can hardly be classified as a stock in trade or as property which would properly be included in the inventory at the close of the taxable year. And the things, like the equipments, machineries and merchandise, including the goodwill, credit and name of the bakery, that went with the sale, were neither property primarily for sale to customers, nor depreciable or real property. Having owned and held said business for more than twelve (12) months, it is urged upon us that only fifty (50%) per centum of the net profit derived from its sale was taxable under Section 34(b) (2) of the Tax Code.

Briefly, respondent maintains that all the rights and interests, consisting of accounts receivable, raw materials, wrapping supplies, firewood, unexpired insurance, machinery, equipment, delivery equipment, and furniture and fixtures, of petitioner in the bakery are ordinary assets for the reason that the same cannot be properly classified as capital assets as contemplated under Section 34(a) of the Tax Code. Accordingly, the net profit realized from the sale under consideration is fully taxable. However, with regard to the goodwill, which was acquired by petitioner in 1951 for ₱10,000.00 and sold in 1955 for the same amount, respondent avers that neither gain was derived, nor loss sustained. Consequently, it is suggested that its sale by petitioner had no material effect on the transaction.

Before considering the issue of whether or not the sale by petitioner of the bakery business in question, a sole proprietorship, was a sale of capital asset, we find it necessary to determine the question of whether the whole business is to be treated as a single property or is to be comminuted into its fragments which should be separately matched against the definition given in Section 34(a) (1) of our Tax Code.

In default of local authorities on the question, we are constrained to look to American precedents, for it is well settled in this jurisdiction that when a law, like Section 34 (a) (1) of our Tax Code which is modelled after Section 117(a) (1) of the U.S. Revenue Codes of 1936, 1938 and 1939, is of American origin, American precedents are in point in determining its construction (Mitsui Bussan Kaisha vs. Hongkong & Shanghai Bank, 36 Phil. 27).

Resolving the question of whether the sale of a going business operated under a single proprietorship should be treated as a sale of a single asset or as a sale of the individual assets comprising the business, the Second U.S. Circuit Court of Appeals, in Williams vs. McGowan, 152 F2d 570, 572 held:

> "x x x. We have to decide only whether upon the sale of a going business it is to be comminuted into its fragments, and these are to be separately matched against the definition in Sec. 117(a) (1), or whether the whole business is to be treated as if it were a single piece of property.
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> "x x x. Be that as it may, in this instance the section itself furnishes the answer. It starts in the broadest way by declaring that all 'property' is 'capital assets', and then makes three exceptions. The first is 'stock in trade x x x or other property of a kind which would properly be included in the inventory'; next comes 'property held x x x primarily for sale to customers'; and finally, property 'used in the trade or business of a character which is subject to x x x allowance for depreciation.' In the face of this language, although it may be true that a 'stock in trade,' taken by itself, should be treated as a 'universitas facti,' by no possibility can a whole business be so treated; and the same is true as to any property within the other exceptions. Congress plainly did not mean to comminute the elements of a business; plainly it did not regard the whole as 'capital assets.'"

The above treatment accorded to the sale of a going business operated under a sole proprietorship found approval in Watson v. Commissioner (1953), 345 U.S. 544, 73 S. Ct. 848, 97 L. Ed. 1232, wherein the U.S. Supreme Court said:

> "The Commissioner's treatment of the proceeds of sales of unmatured crops as ordinary income in the absence of a statutory requirement to the contrary is consistent with the policy evidenced in Williams v. McGowan (NY) 152 F2d 570, 572, 162 ALR 1036, which estab-

lished in the Second Circuit, in 1945, the doctrine that 'upon the sale of a going business it [the sales price] is to be comminuted into its fragments, and these are to be separately matched against the definition in §117 (a) (1) . . .'"

Following the above-quoted American precedents, we hold that the sale of the entire business of petitioner, the "La Suiza Bakery", did not constitute a sale of a single asset. It was a sale of the individual assets comprising the business.

We will now proceed to match the assets, as comminuted in Exhibit 2-E, of the business separately against the codal definition of "capital assets".

The raw materials, wrapping supplies and firewood are properties of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year. Hence, they are ordinary assets. 9 Similarly, the machinery and equipment, delivery equipment, and furniture and fixtures are ordinary assets because they are properties used in the trade or business, of a character which is subject to allowance for depreciation.

The goodwill arising from the sale of the bakery business is a capital asset because it is not a stock in trade of the taxpayer or other property of a kind which is properly includible in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, or property used in his trade or business of a character which would be subject to any allowance for depreciation (Violet Newton v. Commissioner, (1949) 12 TC 204, 208, citing Aaron Michaels, 12 TC 17; Rainier Brewing Co., 7 TC 162, affd, 165 F 2d 217, rehearing denied (C.C.A., 9th Cir.), 166 Fed (2d) 324, Ensley Bank & Trust Co. v. U.S., 61 F Supp. 317, affd, 154 F 2d 968; certiorari denied, 329 U.S. 732; see also Cox et al. vs. U.S. (1951), 99 F Supp 518, 520; Cohen v. Kelm (1953) 119 F. Supp. 376. Ordinarily, goodwill is not subject to depreciation or obsolescence allowances, due to the indefinite duration of its effective usefulness (Mertens, Law of Federal Income Taxation, Vol. 4, sec. 23.10, p. 16).

The accounts receivable are capital assets. While they represented petitioner's business capital, yet, they were not a part of his stock in trade (Max Torodor, et al. vs. Commissioner, 19 TC 530, citing Graham Mill & Elevator Co. v. Thomas 152 F2d 564; see also Rockford Varnish Co. v. Commissioner (1947), 9 TC 171; Estate of Clarence E. Lehr v. Commissioner (1952), 18 TC 373; Levy v. Commissioner (1942) 131 F2d 544; Conrad Hilton et al v. Commissioner (1949) 13 TC 623). They were not held by petitioner primarily for sale to customers in the course of his business, for he was not engaged in the business of selling notes and accounts. He did not have to sell the accounts receivable under consideration, but he merely chose to dispose of them as a part of the ending of his bakery business. Moreover, they are not subject to the allowance for depreciation, neither can they be classified as real property.

The unexpired insurance is a capital asset within the contemplation of Section 34(a) (1) of the Tax Code. Unquestionably, it is not stock in trade of petitioner or property of a kind which would properly be included in his inventory if on hand at the close of the taxable year, or property held by him primarily for sale to customers in the ordinary course of his trade or business, or property, used in the trade or business, of a character which is subject to the allowance for depreciation, or real property.

Proceeding to determine the capital and/or ordinary gains realized by petitioner, we observe that the bases of the assets of the bakery business, as appearing in Exhibit 2-E, are not disputed. However, the gross selling price of all the assets is lumped into ₱100,000.00. And there is no indication what portion of the gross selling price is fairly attributable to each asset, except the goodwill which was bought by petitioner in 1951 for ₱10,000.00 and sold by him in 1955 for the same amount. There being no gain realized or loss suffered from the disposition of the goodwill, this fact does not affect the determination of the capital and/or ordinary gains taxes properly payable on the sale of the other assets of petitioner's business. Consequently, we cannot determine the gain derived or loss sustained from the sale of the other assets. In order to ascertain the capital and/or ordinary gains taxes properly payable on the sale of a business, including its tangible and intangible assets, it is incumbent upon the taxpayer to show not only the cost basis of each asset, but also what portion of the selling price is fairly attributable to each asset (Cohen v. Kelm, supra). In default of such showing, we are constrained to sustain respondent's determination (see Newton v. Commissioner, supra; Green v. Allen, 67 F. Supp. 1004).

FOR ALL THE FOREGOING CONSIDERATIONS, the claim for refund of petitioner against the respondent Collector (now Commissioner) of Internal Revenue in the amount of ₱2,030.00 is hereby denied. Without special pronouncement as to costs.

SO ORDERED.

Manila, August 27, 1959.

MARIANO NABLE
Presiding Judge

I CONCUR:

AUGUSTO M. LUCIANO
Associate Judge

I reserve my vote.

ROMAN M. UMALI
Associate Judge

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