REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

MODESTO T. FLORES, as
Administrator of the Testate
Estate of the late Mary
McDonald Bachrach,
Petitioner,

- versus - C.T.A. CASE NO. 2893

EFREN I. PLANA, in his
capacity as Acting Commissioner
of Internal Revenue,
Respondent.
x - - - - - - - - - - - - - - - x

6/19/81

D E C I S I O N

Under Section 34(a)(1) of the National Internal Revenue Code, real property used in trade or business of the taxpayer and/or which is of a character subject to the allowance for depreciation is not considered a capital asset. Contending that a property consisting of three parcels of land and improvements thereon which the Testate Estate of the late Mary McDonald Bachrach sold in 1970 does not constitute a capital asset because prior to the sale, the said property had been leased to tenants from which rental income was derived and from which yearly depreciation was claimed as deduction, respondent Commissioner of Internal Revenue assessed deficiency income tax against petitioner Modesto T. Flores, as administrator of the Testate Estate of the late Mary McDonald Bachrach, for the year 1974 the amount of ₱113,582.17, computed as follows:

AR-34-1-07013965-74/76

Net income per return - - - - - - - - - -	₱149,640.17
Add: Undeclared income:	
Profit on sale of land & buildings - - - - - - - - - -	138,535.59
Net income per investigation - - - -	₱228,175.76
Less: Personal exemption - - - - - - -	1,800.00
Amount subject to tax - - - - - - - - -	₱286,375.76
Tax due thereon - - - - - - - - - -	₱159,112.00
Less: Amount already assessed - - - -	68,301.00
B a l a n c e - - - - - - - - - -	₱ 90,811.00
Add: 14% int. fr. 4-16-75 to 1-31-77-	22,771.17
TOTAL AMOUNT DUE & COLLECTIBLE - - -	₱113,582.17

Petitioner now seeks the review of the deficiency income tax assessment.

The facts are not in dispute, the parties having entered into a stipulation of facts as follows:

1. That petitioner is the administrator of the Estate of the late Mary McDonald Bachrach duly appointed and qualified as such in Special Proceedings No. 43942 of the Court of First Instance of Manila; while Honorable Efren I. Plana is the duly appointed and qualified Acting Commissioner of Internal Revenue;

2. That the deceased Mary McDonald Bachrach resided abroad until her death sometime in August, 1960, leaving among

her properties, three (3) parcels of land and improvements, (buildings), which were then under construction and completed only in 1962;

3. That the aforementioned properties were leased to Rural Transit, Inc. from 1962 to 1970, and depreciation expenses were claimed from year to year in the income tax returns filed for the Estate of the late Mary McDonald Bachrach;

4. That in September, 1970, the aforementioned properties were sold by the Estate of Mary McDonald Bachrach through its Administrator to Kalayaan Development Corporation on installment basis, the said estate receiving the final payment of ₱500,000.00 in 1974;

5. That the profits derived from the aforestated sale were reported by the estate as capital gains in the income tax returns covering the period in which they were received although depreciation expenses were claimed;

6. That on January 20, 1975, the Court of First Instance of Manila in Special Proceedings No. 43942 issued an Order to the effect that the liability of Bachrach Transportation Co., Inc., owner and operator of Rural Transit, Inc., to the Social Security System for back premium contributions may be enforced against the Estate of the late Mary McDonald Bachrach, the deceased being the majority controlling stockholder of the said Bachrach Transportation Co., Inc. A certified true copy of said Order dated January 20, 1975, is hereto attached and made an integral part of this Stipulation of facts as Annex "A";

7. That as a result of an investigation, herein respondent, on January 31, 1977, issued and sent a letter of demand together with Assessment Notice No.

AR-34-1-07013965-74/76 to Messrs. Flores, Ocampo, Dizon & Domingo, counsel for the Estate of Mary McDonald Bachrach, demanding payment of the sum of ₱113,582.17 as deficiency income tax for 1974 of the said estate, inclusive of 14% interest from April 16, 1975 to January 31, 1977, respondent Commissioner of Internal Revenue having considered the properties sold as an ordinary asset pursuant to Section 34(a)(1) of the Tax Code;

8. That the Estate of Mary McDonald Bachrach through its counsel in its letter dated March 22, 1977, received by the Bureau on March 23, 1977, protested the aforesaid tax assessment;

9. That on August 1, 1977, a copy of the Warrant of Levy on Real Property to enforce collection of the aforestated amount of ₱113,582.17 plus increments thereto incident to delinquency was served upon the Estate through its counsel Messrs. Flores, Ocampo, Dizon and Domingo;

10. That this Stipulation of Facts is without prejudice to the parties' respective claims and defenses and that the parties further reserve their rights to present additional evidence to substantiate their contentions.

The only additional evidence presented by petitioner is Exhibit "A" (p. 61, CTA records), which is the return of previously untaxed income and/or wealth of individuals dated February 28, 1975 filed by the administrator of the Estate of Mary McDonald Bachrach with the Bureau of Internal Revenue under Presidential Decree No. 631. After the parties have filed their respective memorandum, this case was submitted for decision.

As correctly stated by petitioner, the crux of the controversy lies on whether the property sold to the Kalayaan Development Corporation by the Estate of Mary McDonald Bachrach is an ordinary asset or a capital asset pursuant to Section 34(a)(1) of the National Internal Revenue Code. If it is a capital asset, the gain derived from the transaction should be treated as a capital gain, and considering that the property had been held by the Estate for more than twelve months, only 50% of the gain should be taken into account in computing the net capital gain of the Estate for the year 1974, in accordance with the law then in force. On the other hand, if the property sold is considered an ordinary asset, the gain derived therefrom is an ordinary gain, and ordinary gains are taxable in full.

Petitioner's submission that since the improvements, consisting of buildings, made on the three parcels of land left by the deceased Mary McDonald Bachrach were only completed, although started before she died, after her death, there was no business to speak about but only a probate proceeding for the settlement of the Estate which involves nothing more than the payment of its indebtedness and the distribution of the remaining assets among the legatees under the will, hence, there is no property used in trade or business, is positively without basis. Under Section 56 of the National Internal Revenue Code, the estate of a deceased person which is subject of judicial testamentary or intestate proceeding is liable to income tax in the same manner and to the same extent as an individual. It is obvious from the facts of the case, as stipulated by the parties, that the deceased Mary McDonald Bachrach left among her properties three parcels of land and buildings under construction intended for business, as in fact, the said properties, after the construction of the buildings, were rented to the Rural Transit, Inc., from 1962 to 1970; and depreciation expenses were claimed from year to year in the income tax returns filed for the Estate of the deceased, until such properties were sold by the Estate in September 1970, through its administrator, to the Kalayaan Development Corporation on installment basis, the said estate receiving the final payment of ₱500,000.00 in 1974. Since the administrator of the Estate of the late Mary McDonald Bachrach, the settlement of which is the object of testamentary proceeding is required to file an annual return (Sec. 209, Revenue Regulations No. 2) and pay income tax due thereon (Sec. 212, Revenue Regulations No. 2) in the same manner and to the same extent as an individual taxpayer, it must be axiomatic, therefore, that the Estate should pay such taxes upon its transaction, business or income as are imposed by law upon individuals engaged in the same business or transaction.

The controlling statute is Section 34(a)(1) of the National Internal Revenue Code, which textually reads:

> "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."

There is no dispute, and the legal provision applicable seems clear beyond doubt, that under Section 34(a)(1) of the Revenue Code, all property used in trade or business of the taxpayer and/or which is of a character which is subject to the allowance for depreciation does not constitute a capital asset. The gain or loss from the sale or exchange thereof should be treated as ordinary income or loss. Accordingly, if the three parcels of land and buildings which were sold by the Estate of Mary McDonald Bachrach in September 1970 were used by the Estate in trade or business, the gain derived from the sale thereof is ordinary gain, hence, fully taxable. The point then to resolve is whether the leasing of the three parcels of land and the improvements thereon to the Rural Transit, Inc., from 1962 to 1970 and from which depreciation allowance was claimed from year to year in the income tax returns filed by the Estate were used in the trade or business of the latter.

Under the law then in force - Section 194(s) of the National Internal Revenue Code as amended by Republic Act No. 2065, June 22, 1957 - any person engaged in the business of buying, selling, exchanging, leasing, or renting property as principal and holding himself out as a full or part-time dealer in real estate or as an owner of rental property or properties rented or offered to rent for an aggregate amount of ₱4,000.00 or more a year is a real estate dealer. And any person shall be considered as engaged in business as a real estate dealer by the mere fact that he is the owner or sublessor of property rented or offered to rent for an aggregate amount of ₱4,000.00 or more a year.

Here, in the case at bar, it is admitted, and clearly borne by the records, that the deceased Mary McDonald Bachrach left among her properties, three parcels of land located in Caloocan City consisting of 8,181 square meters with an estate inventory value of ₱439,955.00, and improvements which were then under construction at the time of her death sometime in August 1960 but completed in 1962. The improvements consisted of transportation terminal buildings, shop and maintenance buildings, and other building accessories with a construction cost of ₱472,360.01, which by their very nature, were constructed and intended, and actually and purposely, for business and profit. (p. 2, BIR records.) These properties were continuously leased to the Rural Transit, Inc., from 1962 to 1970 from which rental income was derived by the Estate and from which yearly depreciation allowance was claimed as deduction. In September 1970, the aforementioned properties were sold by the Estate of Mary McDonald

Bachrach, through its administrator, to the Kalayaan Development Corporation on installment basis, the said estate receiving the final payment of ₱500,000.00 in 1974.

Since the land and buildings which the Estate sold in 1974 had been leased to the Kalayaan Development Corporation from which rental income was derived and from which yearly depreciation allowance was claimed as deduction, it is self-evident that they cannot be considered as capital asset. Under Section 34(a)(1) of the National Internal Revenue Code, supra, real property used in trade or business of the taxpayer and/or which is of a character subject to depreciation does not constitute a capital asset. The law is clear and specific. It merely calls for application as worded. Where the provision of the law is clear and unambiguous, so that there is no occasion for the court's seeking legislative intent, the law must be taken as it is, devoid of judicial addition or subtraction. (Acting Commissioner of Customs vs. Manila Electric Company, L-23623, June 30, 1977, 77 SCRA 472; Insular Lumber Company vs. Court of Tax Appeals & Commissioner of Internal Revenue, L-31057 & L-31137, May 29, 1981.)

The mere fact that Mary McDonald Bachrach resided abroad until her death, and the business as real estate dealer was engaged in by the Estate through the administrator is of no moment because, as stated earlier, pursuant to Section 56 of the National Internal Revenue Code, the estate of a deceased person is subject to income tax in the same manner and to the same extent as an individual. Where a piece of real property was never occupied by the taxpayer as a residence but was primarily held for rent, it is an ordinary asset as it was used in trade or business, and therefore, the gain derived from the sale of said property is taxable in full. (Collector of Internal Revenue vs. Pedro B. Bautista & Dativa Corrales Tan, L-12250 & L-12259, May 27, 1959, 105 Phil. 1326; Gutierrez vs. Commissioner of Internal Revenue, L-19537, May 20, 1965, 14 SCRA 33.) To the extent that the decision of the Commissioner of Internal Revenue adheres literally to the applicable legal provision, it cannot therefore be assailed as erroneous.

Some stress was placed by petitioner upon the order dated January 20, 1975 of the Court of First Instance of Manila in Special Proceedings No. 43942 to the effect that the liability of the Bachrach Transportation Co., Inc., owner and operator of the

Rural Transit, Inc., to the Social Security System for back premium contributions may be enforced against the Estate of the late Mary McDonald Bachrach, the deceased being the majority controlling stockholder of the said Bachrach Transportation Co., Inc., From this petitioner would want to infer and imply that the deceased Mary McDonald Bachrach and the Bachrach Transportation Co., Inc., operating the Rural Transit, Inc., are one and the same so that no such rental income was actually received by the Estate.

The fallacy of petitioner's argument is its assumption that the order of the Court of First Instance looked beyond the corporate form and ignored the separate entity of the corporations. Whatever the dialectics employed, the Court of First Instance did not treat as identical, one and the same or merged the Estate of the deceased Mary McDonald Bachrach, the Bachrach Transportation Co., Inc., and the Rural Transit, Inc. The basis of the order that the liability of the Bachrach Transportation Co., Inc., to the Social Security System for back premium contributions may be enforced against the Estate of the deceased Mary McDonald Bachrach is merely the majority ownership of the former by the latter - without more. By no stretch of the imagination did the Court of First Instance ruled, or ever implied, that the deceased Mary McDonald Bachrach and the Rural Transit, Inc., are one and the same, so that they should be treated as identical for purposes of taxation. To say therefore"that such rental income was not actually received by the estate" (p. 68, CTA records) is to ignore the basic principle of corporation law that a corporation is an entity separate and distinct from its stockholders and from other corporations.

At any rate, the bare statement of petitioner for the first time in his memorandum "that such rental income was not actually received by the estate" unaccompanied by adequate evidence, when respondent categorically averred in his decision appealed from that "rental income was derived" from the property leased (p. 15, CTA records), has no weight with the Court.

Not much need be said on petitioner's allegation that respondent Commissioner could no longer enforce the assessment in question because the administrator had already availed of the tax amnesty subsequent to the filing of the 1974 income tax return of the Estate which is now being questioned.

(p. 68, CTA records.) While the records show that petitioner has filed a return of previously untaxed income and/or wealth under Presidential Decree No. 631, the disclosure, as explicitly stated therein, refers only to previously untaxed income and/or wealth prior to January 1, 1974 and in the amount of only ₱833.00. (Exh. "A", p. 61, CTA records.) The assessment in question pertains to the tax liability of petitioner for the year 1974 and the amount involved is ₱90,811.00, exclusive of deficiency interest. To quote Section 1 of Presidential Decree No. 631:

> "Section 1. A tax amnesty is hereby granted to any person, natural or juridical, who has not availed of previous amnesty decrees on untaxed income and/or wealth, or having availed thereof, did not made a full and complete disclosure of his untaxed income and/or wealth, or who failed to declare for taxation purposes his true and correct income or receipts earned or received in 1973, which were taxable under the National Internal Revenue Code, if such person voluntarily renders a return of all untaxed income and/or wealth for 1973 and prior years and pay an amount equivalent to twenty (20%) per centum of such untaxed income and/or wealth." (Emphasis supplied)

Clearly, therefore, the voluntary disclosure and rendering of a return of untaxed income and/or wealth of the Estate of Mary McDonald Bachrach pursuant to Section 1 of Presidential Decree No.

631 has no effect on the deficiency income tax assessment for the year 1974 against the same estate involved in this proceeding.

Nor will the argument that the Commissioner of Internal Revenue is estopped from treating the profits derived from the sale of the property as ordinary gains considering that the same have been successively declared in the Estate's annual income tax returns for the last four or five years as capital gains and the same had never been questioned by respondent (pp. 68-69, CTA records), carry the day for petitioner. As aptly stated by respondent, the Commissioner of Internal Revenue is not prevented from rectifying the error and subsequently correctly applying the law, for it is a well-settled doctrine that the Government is not estopped by the mistake or error on the part of its agents. (Pineda vs. Court of First Instance of Tayabas, 52 Phil. 803; Philippine Long Distance Telephone Company vs. Collector of Internal Revenue, 90 Phil. 676.)

We look in retrospect at the philosophy behind the Government's exception from the operation of the principle of estoppel by quoting from the pronouncements of the Supreme Court in Atlas

Consolidated Mining & Development Corporation vs. Commissioner of Internal Revenue, L-26911 and Commissioner of Internal Revenue vs. Atlas Consolidated Mining & Development Corporation and Court of Tax Appeals, L-26924, January 27, 1981:

> "As held in the case of Vera vs. Fernandez, G.R. No. L-31364, March 20, 1979, 89 SCRA 199, this Court emphatically said that taxes are the lifeblood of the Government and their prompt and certain availability are imperious need. Upon taxation depends the Government's ability to serve the people for whose benefit taxes are collected. To safeguard such interest, neglect or omission of government officials entrusted with the collection of taxes should not be allowed to bring harm or detriment to the people, in the same manner as private persons may be made to suffer individually on account of his own negligence, the presumption being that they take good care of their personal affair. This should not hold true to government officials with respect to matters not of their own personal concern. This is the philosophy behind the government's exception, as a general rule, from the operation of the principle of estoppel."

The net result is that the judgment under review must have to be sustained. Accordingly, petitioner Modesto T. Flores, as administrator of the Testate Estate of the late Mary McDonald Bachrach, is hereby ordered to pay to respondent Commissioner of Internal Revenue the sum of ₱113,582.17 as deficiency income tax for the year 1974, plus the 5% surcharge and 14% interest per annum from January 31, 1977 up to January 31, 1980, in accordance with Section 51(e) of the National Internal Revenue Code, as amended.

WHEREFORE, the decision appealed from is hereby affirmed at petitioner's costs.

SO ORDERED.

Quezon City, Metro Manila, June 19, 1981.

Amante Filler

AMANTE FILLER
Presiding Judge

WE CONCUR:

CONSTANTE C. ROAQUIN
Associate Judge

ALEX Z. REYES
Associate Judge