REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
MANILA

ALFONSO ZOBEL, Petitioner, - versus - COMMISSIONER OF INTERNAL REVENUE, Respondent. x - - - - - - - - - - - - - - - - - x	C.T.A. CASE NO. 622
ENRIQUE ZOBEL, Petitioner, - versus - COMMISSIONER OF INTERNAL REVENUE, Respondent. x - - - - - - - - - - - - - - - - - x	C.T.A. CASE NO. 623
JACOBO ZOBEL, Petitioner, - versus - COMMISSIONER OF INTERNAL REVENUE, Respondent. x - - - - - - - - - - - - - - - - - x	C.T.A. CASE NO. 624

D E C I S I O N

Petitioners in the above entitled cases seek to recover sums of money alleged to have been erroneously or illegally collected from them as income taxes for different tax years. In view of the identity of facts and issues involved, these three cases have been jointly submitted for decision of the Court.

The pertinent facts in all these cases are not disputed. It appears that petitioners Alfonso Zobel, Enrique Zobel and Jacobo Zobel, who were all business executives or directors by vocation, duly filed their income tax returns for the tax years in question, on the bases of which they paid income taxes. After an investigation of their income tax liabilities, the respondent Commissioner assessed deficiencies against:

Alfonso Zobel - ₱4,712.00, ₱1,670.00, ₱2,182.00, ₱16,761.00 and ₱5,517.00 for the tax years 1951, 1952, 1953, 1954 and 1955, respectively; Enrique Zobel - ₱29,400.00 and ₱15,278.00 for 1954 and 1955, respectively; and Jacobo Zobel - ₱11,217.00 for 1951. These deficiency assessments were paid and demands for the refund of the payment were made upon respondent, who has not complied with said demands. Hence, the instant appeal.

These deficiencies arose from the treatment by respondent of the gain derived from the sale of petitioners' lands as ordinary and, therefore fully taxable, in contra-distinction to the view that the same is capital and, as indicated in petitioners tax returns, taxable only to the extent of 50%.

It appears that the Hacienda Calatagan of which the lands in question were portions has been the property of the Zobels since 1837. Upon the death of their father in 1943, Alfonso Zobel and Jacobo Zobel inherited it. And in 1951, Jacobo Zobel sold a portion of his share in the hacienda to his son, Enrique Zobel.

Sometime in 1949, tenants in the hacienda and other residents of the municipality of Calatagan organized themselves into a tenants' association and affiliated themselves with the National Federation of Tenants' Association, through which they petitioned the Rural Progress Administration to expropriate the hacienda. Upon like petition, the Provincial Board of Batangas passed a resolution requesting the Provincial Fiscal to take the necessary steps to expropriate the same. The petitioners resisted the demand for expropriation until it came to pass that the peace and order of the municipality was endangered. Upon intercession of the Provincial Governor of Batangas and the municipal mayor of Calatagan, petitioners acceded to the petition for expropriation and in accordance with the compromise entered into with the Rural Progress Administration, a part of the hacienda was subdivided into lots and sold to the tenants and other residents of Calatagan in cash or on installment basis.

The issue in these cases is whether the lands, which were subdivided and subsequently sold, are capital assets so that the gain or profit realized from the sale constitutes capital gain taxable to the extent of 50% only.

Section 34(a)(1) of the Tax Code defines capital assets thus:

> "(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."

Clearly, the lands in question are neither stock in trade nor property of a kind which would properly be included in the inventory if on hand at the close of the taxable year. Similarly, they are not depreciable properties used in trade or business. Consequently, this leaves us to the determination of whether said properties were held by petitioners primarily for sale to customers in the ordinary course of their trade or business, or whether the same are used in the trade or business of petitioners.

The properties under consideration were agricultural; they were acquired by petitioners by inheritance and not by purchase. Until their subdivision and sale, they had been in the possession of the Zobels since 1837. Their sale was forced by the tenants and residents of Calatagan. It was only due to the intercession of the Provincial Governor and the municipal mayor of Calatagan and petitioners' desire to arrest the deterioration of peace and order in the municipality that petitioners eventually acceded to their sale. Moreover, it should be noted that petitioners were business executives or directors. In addition, Jacobo Zobel is an army officer. Finally, it should likewise be observed that the sale of the properties was limited to tenants and residents of the municipality of Calatagan. All these circumstances disprove the validity of the proposition that the properties in question were held by petitioners primarily for sale in the ordinary course of their trade

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or business or were used in their trade or business. This justifies the capital asset treatment of the properties. Judicial pronouncements in the United States sustain this particular view, as shown in the following cases:

DANIEL W. ELLIS ET AL v. COMMISSIONER
(54,021 P-H Memo TC)

In 1935, petitioner inherited from his father 166 acres of land devoted to agriculture. In 1946, he subdivided 44 acres of the land into 72 lots for home building. Sales of the lots were advertised and of the 72 lots 52 were sold. The Court, after considering the nature of the property (agricultural), the manner it was acquired by taxpayer, and sales activity he has displayed and those acting on his behalf, held:

> "x x x. Considering all these activities and the tests which have been developed to aid in determining whether one is engaged in a trade or business within the meaning of section 117 (j) of the Code, we find that the petitioner was not so engaged, and, consequently, the petitioners are entitled to treat the gain realized from the sales of real property as gains from the sale of capital assets held for more than six months."

YUNKER vs. COMMISSIONER
(1 AFTR 2nd 1559)

The taxpayer inherited 75 acres of farm land from her grandfather and uncle and at first attempted to sell it in whole thru a broker. Upon failure to do so, she subdivided it into smaller lots of five acres each and constructed roads thereon to make them salable. Twelve sales were made in 1950 and five in 1951. It was held that the gains realized constituted gains from the sale of capital asset and taxable at long term capital gains rates. The pertinent portion of this decision states:

> "In the latest case to come to our attention, Scott v. McCrory, ___F. Supp ___ (#73,056 P-H Fed. 1957) it was held that a real estate dealer, who inherits land, and who sells it in various tracts, is not, by virtue of his being in the real estate business, thereby precluded from capital gains treatment. In deciding the case, the court said that there was logical reason why one cannot be engaged in the task of disposing property owned by himself, and, at the same time, not be considered to have held it for sale to customers in the ordinary course of his business. The fact that one who is <u>a realtor inherits real estate does not affect the essential character of his activities with relation to the land which he inherited</u>; and if, those activities are found primarily to be liquidating in nature, the transaction in so far as the heirs are concerned are capital, and his status as one is not thereby jeopardized. Hence he is entitled to preferential treatment provided under Section 117. We so hold."
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> "<u>It is our conclusion therefore, that where a person desires to dispose of inherited land, and finds that he can do advantageously only by having it sold in smaller parcels through a real estate dealer, who, to make the property salable, builds a road to give access to it, he may not be denied the right to capital gains treatment by forced construction of the statute to the effect that the land in question was held by the heir primarily for sale to the customers in the ordinary course of his trade or business</u>."

The case of Ramirez v. Commissioner of Internal Revenue, C.T.A. Case No. 544, September 14, 1959, cited by respondent, is not authoritative on this point. In said case, the land and the building thereon were commercial, and, therefore, essentially rental properties.

The properties in the cases at bar are agricultural. The income that petitioners received therefrom was not rent, but their share in the crops raised by the tenants.

WHEREFORE, the respondent Commissioner of Internal Revenue is hereby ordered to refund to petitioner Alfonso Zobel the sums of ₱4,712.00, ₱1,670.00, ₱2,182.00, ₱16,761.00 and ₱5,517.00 or a total of ₱30,842.00; to Enrique Zobel, ₱29,400.00 and ₱15,278.00 or a total of ₱44,678.00; and to Jacobo Zobel, the amount of ₱11,217.00, without special pronouncement as to costs.

SO ORDERED.

Manila, April 29, 1961.

MARIANO NABLE
Presiding Judge

I CONCUR:

ROMAN M. UMALI
Associate Judge

Associate Judge AUGUSTO M. LUCIANO
is on leave.

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