Sibram

REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
Manila

PEOPLES BANK AND
TRUST COMPANY,
Petitioner,

Dec. 14, 1962

- versus -

C.T.A.
CASE NO. 1112

THE COMMISSIONER OF
INTERNAL REVENUE,
Respondent.

x - - - - - - - - - - x

D E C I S I O N

The respondent assessed against the petitioner the sum of ₱251,479.02 as deficiency income tax, surcharge and interest for the year 1951. This deficiency assessment was brought about by the disallowance by respondent of the sum of ₱1,678,872.66 which was claimed by petitioner as war losses in its income tax return for 1951.

It appears that petitioner, a banking and trust corporation, sustained considerable losses during the last war. Immediately after the war, there was doubt as to when such losses could be deducted from the gross income of a taxpayer for purposes of the income tax. The matter was submitted to the Secretary of Finance who rendered an opinion which was embodied in General Circular No. V-123 of the Bureau of Internal Revenue, dated September 18, 1951. Petitioner claimed as a deduction in its income tax return for 1951 a portion of its war losses in the sum of ₱1,678,872.66 in accordance with said circular. Subsequently, a controversy arose as to the correctness of the said opinion of the Secretary of Finance so that the matter was submitted to the Secretary of Justice for opinion. The Secretary of Justice expressed the view that losses sustained during the war were deductible only in the year sustained and not thereafter. Consequently, General Circular No. V-123 was revoked by General Circular No. V-139, dated August 30, 1952. Pursuant to this circular, respondent made the questioned deficiency assessment against petitioner resulting from the disallowance of the said war losses. The deficiency assessment was made sometime in August, 1960. Petitioner contested the assessment on the grounds that the war losses deducted in its 1951 income tax return were properly claimed as a deduction in said year and that, assuming the impropriety of said deduction, the right to assess the said deficiency assessment is already barred by the statute of limitation. Having failed to secure a reconsideration of respondent's decision, petitioner has appealed.

With respect to the issue of prescription, it is contended on behalf of respondent that although the deduction for war losses was properly claimed in petitioner's 1951 income tax return at the time it was filed in February, 1952 because of General Circular No. V-123, the subsequent revocation of said circular by General Circular No. V-139 made it necessary for petitioner to have amended its return. In fact, it was alleged that petitioner was advised by its accountants, Guzman, Bocaling & Co., on October 25, 1956, to file an amended return to eliminate the deduction for war losses. For allegedly deliberately ignoring the advice of its accountants, the income tax return of petitioner for 1951 became fraudulent, thereby making it liable for the fraud penalty. Petitioner's 1951 income tax return being fraudulent, the right to assess the deficiency income tax on the basis of said return is governed by Section 332 of the National Internal Revenue Code which authorizes assessment within ten years from the date of discovery of the fraud. We quote from the decision of respondent:

> "You also alleged that, granting that the war losses sustained by the bank during the war are not deductible in 1951, our right to assess the deficiency income tax for said year has already prescribed for the reason that the 1951 income tax return is not fraudulent and, therefore, the ten year period prescribed under Section 332 of the Tax Code will not apply. It appears, however, that the bank sought the expert advice of its tax consultant and auditor, Guzman, Bocaling & Co., as to the war losses it claimed as deduction in 1951 and that the bank was advised to amend its 1951 return in order to exclude the deduction of the war losses. Despite the written advice of its tax consultant and auditor and the warning to the bank of the 'risks' and 'complications' that may arise in the event that it failed to amend its 1951 return, the bank failed to amend its 1951 return. Such facts clearly, point to the conclusion that the return is fraudulent and that, therefore, the 50% surcharge should be imposed. Thus in a leading case decided in the United States, the 50% fraud penalty imposed against the petitioner was sustained by the Tax Court for deliberately ignoring the expert advice of its counsel -

> 'x x x - Although petitioner was advised by its attorney and accountant in December, 1945, that amended returns should be filed disclosing the unreported income and that any additional tax should be paid as promptly as possible, no such action was taken at that time. x x x only at a later time when there was reason to believe that a revenue agent was hot on the trail.' (George M. Still, Inc. v. Com. of Int. Rev., 19 TC 1077.). (See pp. 180-181, BIR records.)

It is not disputed that petitioner's 1951 income tax return as filed in February, 1952 was not false or fraudulent because it was filed in accordance with an opinion of the Secretary of Finance and the instructions contained in General Circular No. V-123 of the Bureau of Internal Revenue. It was filed in good faith without any intention to evade tax. The sole basis of respondent's decision is that petitioner failed to heed the advice of its accountants in the matter of filing an amended return, citing the case of George M. Still, Inc. v. Commissioner, 19 T.C. 1077.

We think there has been a mistake in the appreciation of the facts and the conclusion reached by the Tax Court of the United States in the case of George M. Still, Inc. In that case, the return as originally filed by the taxpayer was false and fraudulent with intent to evade tax. The underdeclaration which gave rise to the deficiency tax was known to the officers of the corporation at the time the return was filed. When this information became known to its accountants, the latter advised the taxpayer to amend its return. It did not do so until it was advised that an internal revenue agent would examine its books. The U. S. Tax Court rightly held that the taxpayer was guilty of fraud. The fact that the taxpayer failed to amend its return promptly after the advice of its accountants was received merely strengthened the conclusion that the return as originally filed was fraudulent with intent to evade tax. Here is what the U. S. Tax Court said:

> "Petitioner is a corporation, and as such can act only through its officers. During the taxable year ended July 31, 1945, Sidney Still was its president and treasurer, Nancy its vice president, and Michael its secretary. All three were aware, prior to the close of the taxable year and prior to the filing of the original corporate returns, that all sales were not reflected on its books. Despite this knowledge on the part of these officers, the corporation filed tax returns in which this unrecorded income was not disclosed. These returns were signed by Sidney Still as president and treasurer and notarized by Michael Weissman. Although petitioner was advised by its attorney and its accountant in December 1945, that amended returns should be filed disclosing the unreported income and that any additional taxes should be paid as promptly as possible, no such action was taken at that time. Amended returns were filed and additional taxes paid only at a later time when there was reason to believe that a revenue agent was hot on the trail.
>
> "The uncontroverted facts produced in this proceeding clearly support the conclusion that the petitioner willfully and fraudulently, with intent to evade tax, failed to report its true and correct income for its fiscal year ended July 31, 1945, in the original returns filed by it for that year. It follows that petitioner is liable for the 50 per

> cent additions to tax for fraud determined by the respondent." (19 T.C. 1077-1078; emphasis supplied.)

Undoubtedly, the opinion of the U. S. Tax Court in the case of George M. Still, supra, Inc. is inapplicable to the case at bar. The rule as regards the duty of filing amended returns in relation to the fraud penalty has been correctly stated in Mertens' Law of Federal Income Taxation as follows:

> The failure to file an amended return to correct an accounting error in the original return is not proof of fraud. Sam E. Broadhead, TC Memo, 1955-328. (Mertens, Vol. 10, Sec. 55.-10, note 92, p. 64.)

> Subsequent conduct of the taxpayer, after the filing of the return, even though reprehensible, will not justify the imposition of the penalty, unless the fraudulent intent is shown to have existed when the return was filed. (Mertens, Vol. 10, Sec. 55.12, p. 67.)

Then, too, the records show that in this case while petitioner was advised by its accountants to file an amended return, it received a contrary advice from its legal counsel. The question in regard to the deductibility of war losses in the year other than when they were actually sustained is purely a question of law. Petitioner was entitled to heed the advice of its legal counsel and not that of its accountants.

Having arrived at the conclusion that petitioner's income tax return for 1951 was not filed fraudulently with intent to evade tax, the right of the Government to assess deficiency income tax on the basis of said return expired after five years from the date the return was filed or was due, pursuant to Section 331 of the Revenue Code.] The deficiency assessment in this case was made after more than eight years. Therefore, the right of the Government to assess the said deficiency tax has prescribed. Consequently, we find it unnecessary to pass upon the other issue as to the legality of the deduction in question. It has also become unnecessary for petitioner to file a surety bond required in our resolution of November 14, 1962 as a condition for the suspension of the collection of the tax by respondent pending appeal.

WHEREFORE, the decision appealed from is reversed, without pronouncement as to costs.

SO ORDERED.

Manila, December 14, 1962.

ROMAN M. UMALI
Associate Judge

WE CONCUR:

MARIANO NABLE
Presiding Judge

AUGUSTO M. LUCIANO
Associate Judge