REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

BRIXTON INVESTMENT
CORPORATION
JOSE MA. BARCELON
TERESITA BARCELON
ROSITA BARCELON
ANGELITA BARCELON
LUIS BARCELON
EMETERIO BARCELON, JR.,
Petitioners,

April 18, 1967

-versus C.T.A. CASE NO. 1681

BENJAMIN TABIOS, as
COMMISSIONER OF INTERNAL
REVENUE,
Respondent.
x- - - - - - - - - - - - - -x

# D E C I S I O N

This is an appeal from the decision of respondent assessing against and demanding upon petitioners, namely: Brixton Investment Corporation, Jose Ma. Barcelon, Teresita Barcelon, Rosita Barcelon, Angelita Barcelon, Luis Barcelon and Emeterio Barcelon, Jr., payment of deficiency income tax and interest for 1957 in the amounts of ₱18,994.46, ₱1,164.66, ₱831.90, ₱600.62, ₱597.08, ₱541.62 and ₱154.40, respectively. In addition, Emeterio Barcelon, Jr. was assessed for deficiency income tax, interest, surcharge and penalty for 1956 in the aggregate sum of ₱122.75. (Exh. K, CTA Rec. pp. 45-50)

Petitioner Brixton Investment Corporation (hereinafter referred to as Corporation) is a duly registered domestic corporation. In 1957, the Corporation was principally engaged in business as a real estate dealer (income from leasing real property) and also in the sale of real estate, purchase and sale of securities, and in the placement of short-term deposits with banking and financial institutions. For the year in question, the Corporation declared in its income tax return a gross income of ₱309,309.66 consisting of ₱172,253.38, ₱134,500.03, ₱1,356.25 and ₱1,200.00 as income from the sale of two (2) pieces of real estate, leasing of real properties, dividends, and income from Limpan Investment Corporation. From the gross income of ₱309,309.66, the Corporation made a total deduction of ₱217,310.10 thereby leaving a net taxable income of ₱91,999.56. (Exh. D, CTA Rec. pp. 28-29). It is to be noted that in the first sale of the land and building, the Corporation realized a gain of ₱193,181.80 in 1957. In the sale of real property to Emeterio Barcelon, Sr. for the same year, the Corporation suffered a loss of ₱20,928.50, thereby leaving an income of ₱172,253.38 from the two sales of real estate. (Exh. D, id.)

The other petitioners Jose, Teresita, Rosita, Angelita, Luis and Emeterio, Jr., all surnamed Barcelon, are brothers and sisters and all of them are stockholders and officers of the Corporation with the exception of Emeterio Barcelon, Jr., who is not an officer thereof. It will thus be seen that Brixton Investment is a family corporation. In fact, its 6,000 shares of stock valued at ₱600,000.00, or ₱100.00 per share of stock, are owned by the above-named brothers and sisters with the exception of two (2) shares of stock which were registered in the name of Atty. Gelasio L. Dimaano, Secretary and Legal Counsel of the corporation - one (1) share; and Ms. Pilar Sarquesta - one (1) share.

For the taxable year 1957, petitioners filed their individual income tax returns on or before March 1, 1958 with the exception of Emeterio Barcelon, Jr. The said income tax returns were examined, verified and investigated by a set of revenue examiners simultaneously with the investigation of the corporate income tax return of the Corporation for the same year. On the basis of their findings and report, respondent sent a letter of assessment and demand to all the petitioners, dated May 31, 1962, calling for the payment of their 1957 deficiency income tax listed as follows:

| | |
|---|---|
| Brixton Investment Corporation .. | ₱20,010.87 |
| Jose Ma. Barcelon ............... | 4,535.49 |
| Teresita Barcelon ............... | 3,299.87 |
| Rosita Barcelon ................. | 2,785.73 |
| Angelita Barcelon ............... | 2,777.07 |
| Luis Barcelon ................... | 2,633.72 |
| Emeterio Barcelon, Jr. ......... | 2,056.28 |

(Exh. J, CTA Rec. pp. 41-44)

Respondent also assessed Emeterio Barcelon, Jr. for deficiency income tax, surcharge, interest and penalty for 1956 in the total amount of ₱122.75.

On June 1, 1962, petitioners' counsel requested respondent to reconsider the above-listed deficiency income tax assessment. In a letter of respondent to petitioners' counsel dated January 25, 1963 (Exh. K, id.), the previous deficiency income tax assessment against petitioners for 1957 (Exh. J, id.) was revised and reduced as follows:

| | |
|---|---|
| Brixton Investment Corporation .. | ₱18,994.46 |
| Jose Ma. Barcelon .............. | 1,164.66 |
| Teresita Barcelon .............. | 831.90 |
| Rosita Barcelon .............. | 600.62 |
| Angelita Barcelon .............. | 597.08 |
| Luis Barcelon ............... | 541.62 |
| Emeterio Barcelon, Jr. ......... | 154.40 |

Again, Emeterio Barcelon, Jr. was required to pay the 1956 deficiency income tax, surcharge, interest and penalty of ₱122.75.

The deficiency income tax of ₱18,994.46 assessed against the Corporation was partly due to the total or partial disallowance of the deduction from gross income of the salaries of its officers amounting to ₱46,400.00, computed as follows:

| Name | Position | Salaries Declared | Salaries Allowed | Salaries Disallowed |
|---|---|---|---|---|
| Jose Barcelon | President | ₱9,600.00 | ₱2,400.00 | ₱7,200.00 |
| Luis Barcelon | Vice-Pres. | 8,500.00 | 1,800.00 | 6,700.00 |
| Teresita Barcelon | Treasurer | 9,600.00 | --- | 9,600.00 |
| Rosita Barcelon | Asst. Treasurer | 7,200.00 | --- | 7,200.00 |
| Emeterio Barcelon, Sr. | Chairman of the Board | 6,000.00 | 4,800.00 | 1,200.00 |
| Angelita Barcelon | Asst. Secretary | 8,400.00 | --- | 8,400.00 |
| Gelacio Dimaano | Sec. & Legal counsel | 8,500.00 | 2,400.00 | 6,100.00 |
| | | ₱57,800.00 | ₱11,400.00 | ₱46,400.00 |

As to the deficiency income tax assessed by respondent against the Barcelon brothers and sisters, it was based on the findings and report of the revenue examiners that the Corporation had a surplus of ₱24,758.87 in 1957. This surplus was considered by respondent as cash dividend paid to the Barcelon brothers and sisters in the proportion of ₱4,126.47 each.

On February 28, 1963, petitioners further requested respondent to reconsider his revised and reduced deficiency income tax assessment but said request was denied by respondent in his letter to petitioners' counsel dated July 8, 1965. Hence, petitioners appealed to this Court by filing their petition for review on August 28, 1965. On December 14, 1965, respondent filed his answer thereto.

The issues raised by the opposing parties and submitted for the resolution of the court are the following:

1. Whether or not the right of respondent to assess and collect the deficiency income taxes of petitioners for 1957 has prescribed under Section 331 of the National Internal Revenue Code, in relation to Section 332 of the same Code;

2. Whether or not the deduction of ₱46,400.00 from the 1957 gross income of the Corporation, representing salaries of its officers which were disallowed by respondent, is legal and justified under Section 30(a)(1) of the National Internal Revenue Code, in relation to Section 70 of the Income Tax

Regulations;

3. Whether or not the inclusion by respondent of ₱4,126.47 as dividend income to the 1957 net income of each of the Barcelon brothers and sisters is legal and justified; and

4. Whether the amount of deficiency income tax assessed by respondent against Jose Ma. Barcelon for 1957 was ₱4,526.00 or ₱4,306.00.

First Issue

Petitioners claimed that the disputed deficiency income tax for 1957 was not assessed by respondent within the period prescribed by Section 331 of the National Internal Revenue Code. (Par. X, Petition for Review, CTA Rec., p. 3). However, petitioners' counsel abandoned the defense of prescription of assessment alleged in the petition for review but instead invoked in his memorandum the defense of prescription of collection. (See CTA Rec., pp. 86-90). In short, petitioners considered that, even if the disputed tax assessment were valid and legal, the right of respondent to collect from petitioners their deficiency income tax for 1957 has prescribed under Section 332(c) of the Revenue Code, in relation to Section 331 of the same Code which reads as follows:

> "SEC. 331. Period of limitation upon assessment and collection.- Except as provided in the succeeding section, internal-revenue taxes shall be assessed within five years after the return was

filed, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period. For the purposes of this section a return filed before the last day prescribed by law for the filing thereof shall be considered as filed on such last day. xx xx.

"SEC. 332. Exceptions as to period of limitation of assessment and collection of taxes.-

xx xx xx

(c) Where the assessment of any internal-revenue tax has been made within the period of limitation above-prescribed such tax may be collected by distraint or levy or by a proceeding in court, but only if begun (1) within five years after the assessment of the tax, xx xx."

Petitioners alleged that their income tax returns for 1957 were filed with respondent on March 1, 1958; the tax due thereon was assessed by respondent on June 29, 1960 (Exh. 16, BIR Rec., pp. 105-106); the petition for review was filed by petitioners with the court on August 28, 1965; and the answer thereto of respondent was made on December 13, 1965. On the basis of said allegations, petitioners concluded that the right of the Government to collect the tax under Section 332(c) of the Revenue Code, supra, has prescribed because from June 29, 1960 (date when the alleged income tax assessment dated June 14, 1960 was received by petitioners) to December 13, 1965 (date when the answer to the petition for review was made by respondent), more than five years and five months have elapsed.

We cannot subscribe to the defense of prescription of collection invoked by the petitioners. It is to be noted that respondent's letter to petitioners dated June 14, 1960 (Exh. 16, BIR Rec., pp. 105-106) is not the tax assessment referred to and contemplated in Section 331 of the Revenue Code, supra. The tax assessment mentioned therein means an outright or final internal-revenue tax assessment and not a proposed tax assessment. A careful examination and analysis of the letter in question will show that it is not a formal assessment of the tax sought to be collected or a demand-letter for the collection thereof. On the contrary, the aforesaid letter to petitioners is merely a proposed tax assessment of the investigating revenue examiners requesting petitioners to interpose their objections thereto and present their evidences against the same; otherwise, the tax assessment mentioned and referred to in Section 331 of the Revenue Code will be issued by respondent against petitioners.

In the case at bar, the deficiency income tax assessment was issued by respondent against petitioners on May 31, 1962 (Exh. J, CTA Rec., pp. 41-44) and not in June of 1960. It was disputed by the petitioners in a letter to respondent dated June 1, 1962. On January 25, 1963, a revised deficiency income tax assessment was issued by respondent against the petitioners. (Exh. K, CTA Rec., pp. 45-50). This is the final deficiency income tax assessment for purposes of computing the prescriptive period of assessment referred to in Section 331 of the Revenue Code. (See Ker & Co. vs. Collector of Internal Revenue, CTA Case No. 244, January 5, 1957, aff'd in G.R. No. L-12396, January 31, 1962; and Commissioner of Internal Revenue vs. Carlos Moran Sison, et al., G.R. No. L-13739, April 30, 1963). It is clear, therefore, that the final tax assessment was issued by respondent in 4 years, 10 months and 24 days from the date petitioners filed their income tax returns on March 1, 1958 to January 25, 1963 when the final assessment was made.

The final tax assessment having been issued by respondent on January 25, 1963, under Section 332(c) of the Revenue Code, supra, the right of the Government to collect the tax in question must be made within five years from that date. Consequently, as the appeal of petitioners from the disputed assessment was filed in court on August 28, 1965, which appeal is considered the beginning of the judicial action for the collection of the tax (Collector of Internal Revenue vs. Bohol Land Transp. Co., G.R. Nos. L-13099 & L-13462, April 29, 1960), the right of respondent to collect the 1957 deficiency income tax of petitioners has not prescribed.

Second Issue

Petitioners contend that the salaries of ₱46,400.00

paid to the officers of the Corporation, namely:

Jose Ma. Barcelon ........President
Luis Barcelon ............Vice-President
Teresita Barcelon ........Treasurer
Rosita Barcelon ..........Asst. Treasurer
Gelasio Dimaano ..........Secretary & Legal Counsel
Angelita Barcelon ........Asst. Secretary

should be allowed as a deduction from gross income because the said salaries of ₱46,400.00 are reasonable and paid for services rendered by each of them. Respondent contends, however, that the salaries in question are excessive, unreasonable, and paid for services which were not actually rendered by some of the corporate officers. The excess and unjustified payment of salaries were treated by respondent as a distribution of the corporate earnings which formed part of the petitioners' gross income as defined in Section 29(a) of the Revenue Code.

The general and specific requirement for the deduction of salaries or other compensation from gross income is embodied in Section 30(a)(1) of the Revenue Code which provides, among others, as follows:

> SEC. 30. Deductions from gross income.- In computing net income there shall be allowed as deductions -
>
> (a) Expenses:
>
> (1) In general.- All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; x x."

Under the foregoing provisions of law, the deductibility of salaries from gross income must meet and comply with the following requisites, to wit:

1. The expense for salaries must be both ordinary and necessary;

2. The salaries must be paid or incurred within the taxable year;

3. The salaries must be incurred in carrying on a trade or business;

4. The expense must in fact be salaries or other compensation;

5. The salaries must be for personal services actually rendered; and

6. The salaries must be reasonable in amount.

In implementing the provisions of Section 30(a)(1) of the Revenue Code, supra, as authorized by Section 338 of the same Code, the Secretary of Finance promulgated Revenue Regulations No. 2, otherwise known as the Income Tax Regulations. Section 70(1) thereof provides as follows:

> SEC. 70. Compensation for personal services.- Among the ordinary and necessary expenses paid or incurred in carrying on any trade or business may be included a reasonable allowance for salaries or other compensation for personal services actually rendered. The test of deductibility in the case of compensation payments is whether they are reasonable and are, in fact, payments purely for service. This test and its practical application may be further stated and illustrated as follows:

> (1) Any amount paid in the form of compensation, but not in fact as the purchase price of services, is not deductible. (a) An ostensible salary paid by a corporation may be a distribution of dividend on stock. This is likely to occur in the case of a corporation having few shareholders, practically all of whom draw salaries. If in such a case, the salaries are in excess of those ordinarily paid for similar services, and the excessive payments correspond or bear a close relationship to the stockholdings of the officers or employees, it would seem likely that the salaries are not paid wholly for services rendered, but that the excessive payments are a distribution of earnings upon the stock. (Promulgated Feb. 11, 1941, 39 O.G. No. 18, p. 325)

Respondent contends that the salaries paid to the officers of the Corporation are in excess of those ordinarily paid for similar services. In support of his contention, respondent cited the case of Susana Realty, Inc., a corporation also engaged in leasing real estate properties, regarding the salaries paid to its employees. The facts and figures contained in the report of the investigating revenue examiners, dated April 3, 1962, are as follows:

BRIXTON INVESTMENT, INC.

| Gross Rental Income | Salaries Paid | Percentage of Salaries to Gross Income |
|---|---|---|
| 1954 - ₱190,398.50 | ₱ 77,795.00 | 40% |
| 1955 - 179,468.60 | 85,486.00 | 47% |
| 1956 - 194,549.11 | 99,064.30 | 50% |
| 1957 - 134,500.03 | 79,032.00 | 58% |
| SUSANA REALTY, INC. | | |
| 1956 - ₱1,062,785.31 | ₱155,284.12 | 14% |
| 1957 - 1,132,895.28 | 165,880.95 | 14% |

| | | | |
|---|---|---|---|
| 1958 - | ₱1,464,182.10 | ₱182,845.93 | 12% |
| 1959 - | 2,615,089.76 | 188,890.67 | 7% |

(Exh. 23, p. 184 BIR rec.)

The said report of the revenue examiners shows that Susana Realty, Inc. has 23 and 50 employees in 1956 and 1957, respectively, but it paid to its employees a very much lower percentage of salaries in comparison with its gross income than that of the Corporation (petitioner) despite the fact that Susana Realty, Inc. had a very much bigger income from the lease of its real estate properties. It will be noted that, while the total salaries paid by the Corporation in 1957 amounted to ₱79,032.00, the major portion of the salaries in the amount of ₱57,800.00 were paid to the officers of the Corporation who are stockholders thereof, thereby leaving only ₱21,232.00 as salaries paid to the rest of the employees.

The comparative data of the percentage of the salaries of the employees of Susana Realty, Inc. in proportion to its gross income, which appeared in the report of the revenue examiners, was vigorously assailed by petitioners' counsel on the ground that the testimony of one of the revenue examiners, Melchor Masakayan, is purely hearsay and inadmissible as evidence because neither the books of accounts nor the income tax returns of Susana Realty, Inc. have been produced and submitted to the court. This objection is devoid of merit. In a case involving similar issue, our Supreme Court held as follows:

> "The plaintiff also contended that the affidavits of Sultan Barorao and Liceria Abaden de Pañganiban which contained statements to the effect that they sold cassava tubers to the plaintiff should not have been admitted and the testimony of Internal Revenue agent Artemio Jacalan, was a mere hearsay. This is untenable. The court admitted these affidavits as a part of the testimony of the Internal Revenue agent Jacalan who investigated the matter.
>
> "It should be observed that Republic Act No. 1125, creating the Court of Tax Appeals, expressly provides that the Court shall not be governed strictly by technical rules of evidence (Sec. 8). Therefore, if the said Court believes that the affidavits in question should be admitted, as part of the testimony of the Internal Revenue agent, then it is substantially in conformity with the provisions of Section 8 of Republic Act No. 1125." (Purakan Plantation Company vs. Melecio R. Domingo, G.R. No. L-18571, October 29, 1965; The Philippine Tax Journal, Vol. 11, p. 498.)

Petitioners' counsel also assailed the report and testimony of revenue examiner Masakayan by alleging that the gross income of the Corporation in 1957 was ₱309,309.65 and not ₱134,500.03. It is argued, therefore, that the percentage of salaries paid by the Corporation amounting to ₱79,032.03, in proportion to its gross income, should be 25% only instead of 58% as testified to by the said revenue examiner. We do not share with the view of petitioners on this point. In the first place, the income tax return of the Corporation for 1957 shows that it was principally engaged in leasing real estate properties as its main activity during the year in question. In the second place, the fact that the Corporation realized a substantial income (₱193,181.80) in the sale of real estate and lost (₱20,928.50) in the sale of another property is of no moment in evaluating the reasonableness of the compensation paid to its officers because the said sales were isolated transactions and no evidence was adduced that all the corporate officers participated therein.

As a general rule, the employer is given a wide latitude of discretion in the amount of salaries paid to the employees. A corporation has the right to fix the compensation of its employees (Ledesma vs. Collector of Internal Revenue, 42 Phil. 912), and courts are not inclined to intervene with that right if properly exercised. (Levine & Bros., Inc. v. Commissioner, 101 F (2d); Wagegro Corp., 38 BTA 1225). However, where the question of reasonableness of salaries is put in issue, the burden of proving rests solely on the taxpayer. (Allie Tuberville, 31 BTA 283, aff'd 84 F (2d) 307; Edgar Carnrick, 21 BTA 12, 21; National Contracting Co., 37 BTA 689, aff'd 105 F (2d) 488). These court rulings are particularly applicable in the case of a closely held corporation like the taxpayer. (See

Vol. 4, p. 243, Mertens on the Law of Federal Income Taxation, revised ed.).

Petitioner Jose Ma. Barcelon is the president of the Corporation from June to November, 1957. Before that period, it was Emeterio Barcelon, Sr. who was its president from January to May, 1957. In December of the same year, Jose Ma. Barcelon left for the United States and his brother, Luis Barcelon, discharged the duties of president. (t.s.n., pp. 30 and 40). It is claimed that the salary of ₱9,600.00 paid to Jose Ma. Barcelon as president of the Corporation is reasonable because (1) he is a member of the Manila Stock Exchange since 1955; (2) member of its Board of Governors; (3) president of a brokerage firm; (4) president of the Anglo-Philippine Oil Corp. with ₱2,000.00 a month as representation expenses given to him; (5) director of the Philippine Iron Mines, Inc. from which he received more than ₱11,000.00 per annum as director's fees; and (6) director of the Southern Gold Mines.

As president of the Corporation, Jose Ma. Barcelon supervises its affairs and makes policy decisions therefor. He goes to the office of the Corporation regularly in the morning. Thereafter, he goes to the Manila Stock Exchange at 9:00 A.M. to pursue his own brokerage business. While it is true that he represents and handles the investment of the Corporation in securities in late October, 1957 (t.s.n. pp. 31 and 103), the 1957 income tax return of the Corporation shows that, instead of making profit, it suffered capital losses of ₱71,288.71 in selling securities for that year.

Considering that the petitioner, Brixton Investment Corporation, was principally engaged in leasing real estate properties like the Susana Realty, Inc., its president, Jose Ma. Barcelon, was engaged in other business activities from which he received the greater bulk of his income; he served the Corporation in 1957 as president for only six (6) months; the Corporation is controlled by the members of his family; and the type and extent of services rendered by him to the Corporation appear to be ordinary, we will be constrained to fix the reasonable amount of his compensation based on the evidence of record.

In the last hearing of this case on March 18, 1967, Mr. Jose Laurea, external auditor of Susana Realty, Inc., testified that during the investigation of the income tax case of Brixton Investment Corporation, he gave a list to revenue examiner Melchor Masakayan showing the salaries of the officials and employees of Susana Realty, Inc. for 1957 (t.s.n. p.

159). This testimony of the witness is strengthened by his previous statements under oath. (Exh. 30, CTA Rec., p. 149)

The evidence of record discloses that the salaries received by the ranking officials and employees of Susana Realty, Inc. in 1957 are as follows:

| Name | Position Held | Salary |
|---|---|---|
| Benita B. Arevalo | Chief Accountant | ₱ 5,635.00 |
| Jose F. Jacinto | Construction Engineer | 7,800.00 |
| Jose P. Madrigal | Gen. Manager & Treas. | 7,000.00 |
| Joaquin Mayoralgo | Gen. Superintendent | 7,475.00 |
| Jaime Norit | Surveyor | 5,200.00 |
| Nemesio Sugui | Bookkeeper | 2,275.00 |
| Demetrio Valencia | Madrigal Bldg. Supt. | 2,000.00 |
| Ernesto Villaluz | Lawyer | 2,700.00 |
| Amanda V. Viray | Assistant Counsel | 8,200.00 |

Compared to the 1957 salaries of the Barcelon brothers and sisters, who were officers of the Brixton Investment Corporation (a family corporation), with the officials of Susana Realty, Inc., we find that the salaries paid to the members of the Barcelon family were excessive and unreasonable. In the case of Susana Realty, Inc. its general manager, Mr. Jose P. Madrigal, is at the same time the treasurer thereof. Despite the fact that he holds and discharges the functions of general manager and treasurer of the said corporation, he was only paid a salary of ₱7,000.00 in 1957.

Be that as it may, we do not question that Jose Ma. Barcelon, president of Brixton Investment Corporation, is entitled to a reasonable compensation of ₱9,600.00 per annum. However, inasmuch as he had served the Corporation as its president for a period of six (6) months only, his salary should be fixed at ₱4,800.00 instead of ₱2,400.00 as determined by the investigating revenue examiner.

Emeterio Barcelon, Sr., president of the Corporation from January to May, 1957, was given a compensation of ₱6,000.00 per annum as reflected in the income tax return of the Corporation. Considering, however, that he had served the Corporation as its president for a period of five (5) months only, the salary of ₱4,800.00 fixed by the revenue examiner is deemed fair and reasonable.

The burden of proving the reasonableness of the salaries devolves solely upon the persons who received them. In the case at bar, the other petitioners, namely: Luis, Teresita, Angelita and Rosita, all surnamed Barcelon, were not presented in court as witnesses to show that they, in fact, rendered personal services to the Corporation; the nature, extent and importance of their services; the daily or weekly number of hours spent for their work; and the reasonableness of the compensation paid to them. No evidence was introduced that the positions of vice-president, assistant treasurer and assistant secretary were ordinary and necessary in the business of leasing real estate properties. The number of tenants and the volume, amount and frequency of their transactions with the Corporation were not disclosed in order that this Court can assess the reasonable amount of compensation, if any, due them. In short, the above-named petitioners failed to justify the legality and reasonableness of the compensation paid to them by the Corporation.

The corporate secretary and legal counsel, Atty. Gelacio Dimaano, was not also called by petitioners to testify in court as to the reasonableness of his compensation. He only took care of all controversial matters with the tenants of the Corporation and filed protests with the authorities concerned involving real property tax assessments. (t.s.n., p. 39)

A careful scrutiny of the testimonies of Rosauro Atangan and Jose Ma. Barcelon, accountant and president of the Corporation, regarding the nature, extent and importance of the services rendered by the other corporate officers were made in general terms and vague references. Said testimonies, bare in important and essential details as to the reasonableness of the salaries paid to the other corporate officers, have not helped this Court in arriving at a fair and just conclusion.

Respondent's examiner, however, testified that in 1957, Teresita, Rosita and Angelita, all surnamed Barcelon, were enrolled in a school of nunnery called "Institucion Teresiana". Despite diligent efforts, the said examiner failed to secure from the said institution a certificate that the Barcelon sisters were enrolled therein during the year in question. The examiner tried to bolster his conclusion by alleging that, during the course of his investigation of the Corporation and its officers in 1959, he could not interview or get in contact with the Barcelon sisters. However, without passing upon the intrinsic merit of the testimony of respondent's examiner, we are of the opinion that, after evaluating and sifting the evidence of record, the positions of assistant treasurer and assistant secretary are not necessary in the business set up of the Corporation and that no sufficient evidence was adduced to justify the compensation paid to the occupants thereof.

In the case of Luis Barcelon and Teresita Barcelon, vice-president and treasurer of the Corporation, we have found ample evidence showing that they have rendered personal services to the Corporation in 1957. They are, therefore, entitled to a reasonable amount of compensation. We are also prone to give a reasonable amount of compensation to the corporate secretary and legal counsel, Atty. Gelacio Dimaano.

Considering the facts and circumstances of this case, we hold that, in 1957, the reasonable amount of salaries deductible from the gross income of the Corporation are as follows:

| | | |
|---|---|---|
| Jose Ma. Barcelon | President (6 mos.) | ₱4,800.00 |
| Emeterio Barcelon, Sr. | " (5 mos.) | 4,800.00 |
| Luis Barcelon | Vice-President | 6,000.00 |
| Teresita Barcelon | Treasurer | 6,000.00 |
| Gelacio Dimaano | Sec. & Legal Counsel | 4,800.00 |
| | T O T A L ------------- | ₱26,400.00 |

Out of the total salaries of ₱57,800.00 paid by the Corporation to its officers in 1957, only the sum of ₱26,400.00 is deemed just and reasonable. The balance of ₱31,400.00 being unjustified and unreasonable, the said amount is hereby disallowed as a deduction from the gross income of the Corporation. Consequently, there is due and collectible from the Corporation deficiency income tax and interest in the total sum of ₱10,271.90 arrived at as follows:

Brixton Investment, INC.

1957

| | | |
|---|---|---|
| Net income per 2nd investigation ...... | | ₱155,014.52 |
| Less: Allowable deductions: | | |
| Salaries ........... | ₱26,400.00 | |
| Miscellaneous advances written off ........ | 240.00 | |
| Miscellaneous expenses | 3,000.00 | 29,640.00 |
| Net taxable income .................... | | ₱125,374.52 |

| | |
|---|---|
| Tax due thereon ........................ | ₱ 27,105.00 |
| Less: Amount already assessed ............ | 18,400.00 |
| Balance still due ........................ | 8,705.00 |
| Add: ½% monthly interest from 6-20-59 to 6-20-62 (18%) .................. | 1,566.90 |
| TOTAL AMOUNT DUE AND COLLECTIBLE .......... | ₱ 10,271.90 |

Third Issue

The Barcelon brothers and sisters, namely: Luis, Teresita, Angelita, Rosita, Jose and Emeterio, Jr. have withdrawn money from the funds of the Corporation in 1954, 1955 and 1956. Those withdrawals by the stockholders were treated by respondent's examiners as distribution of cash dividends. As of December 31, 1957, the surplus of the Corporation amounted to ₱127,445.30. Deducting from the said amount the withdrawals made by the said stockholders for prior years, there remained a balance of ₱24,758.87, computed as follows:

| | | |
|---|---|---|
| Surplus, Dec. 31, 1957 as per balance sheet.. | | ₱127,445.30 |
| Less: Withdrawals of prior years treated as dividends: | | |
| 1954 | ₱64,868.70 | |
| 1955 | 9,180.00 | |
| 1956 | 28,737.43 | 102,686.43 |
| Surplus on Dec. 31, 1957 distributed as dividends ........................ | | ₱ 24,758.87 |

The said amount was divided by the revenue examiners among the six stockholders above-mentioned and considered as their additional income in 1957. Hence, the assessment and demand of respondent against them for 1957 deficiency income tax on the theory that dividends on corporate stock are subject to income when unqualifiedly made subject to the demand of stockholder, in accordance with the third paragraph of Section 250 of the Income Tax Regulations which provides:

> SEC. 250. Dividends.- xx xx
>
> A taxable distribution made by a corporation to individual stockholders or members shall be included in the gross income of the distributees when the cash or other property is unqualifiedly made subject to their demand. Dividends, in cash or other property received by an individual, are subject to tax in his hands in the same manner as other income.

Petitioners disputed the view of respondent and alleged that the withdrawals made by them from the funds of the Corporations were loans and not cash dividends. It is therefore necessary to distinguish between dividends and loans to resolve the question here at issue. If the amounts withdrawn by the stockholders from the funds of the Corporation were at the time of withdrawals intended to be repaid, they are considered as loans. (Moses W. Faitoute, 38 BTA 32). But, if the withdrawals are substantially in proportion to stockholdings, especially in a close corporation, and no notes are executed (Jesse B. Hawley, BTA Memo. Opinion, April 29, 1939), no interest is charged or paid, no repayment is made, and no effort is exerted to enforce collection (A. W. Mellon, 36 BTA 977; Roy J. Kinnear, 36 BTA 153), they are held as dividends.

We find that the view of respondent is untenable because the withdrawals made by the Barcelon brothers and sisters from the funds of the Corporation were greatly disproportionate to their individual stockholdings; the withdrawals were recorded in the books of the Corporation as loans and advances receivable (See Exhs. A-1 and B-1, pp. 7 and 9 of Exhs. A and B); and the withdrawals and advances were intended to be repaid.

The withdrawals of the corporate funds, which were considered as loans, are confirmed by the application thereto of the payments made by the Barcelon brothers and sisters of ₱144,000.00, representing the amount of the capital stock of the Corporation which was subscribed and paid by them. The application of said payments was approved and sanctioned in separate resolutions of the Board of Directors and the stockholders of the Corporation, both dated December 28, 1957. (BIR rec., pp. 107-108; t.s.n., pp. 42 and 114). Subsequently, on December 22, 1958, the Barcelon brothers and sisters sold and transferred to the Corporation a lot situated near the Coca-Cola Plant at Valenzuela, Bulacan, for ₱180,000.00. (Exh. C, CTA rec., pp. 26-27). The payments of ₱144,000.00 and ₱180,000.00 were credited in the ledger of the Corporation in 1957 and 1958 against the loans and advances receivable. (See Exhs. A & A-1; and B & B-1). The loans in question cannot therefore be considered as dividends paid to the Barcelon brothers and sisters. As a consequence of our ruling on this point, it follows that the undistributed surplus of the Corporation in 1957 amounting to ₱24,758.87 can not be a distribution of dividends to the Barcelon brothers and sisters. Accordingly, we hold that they are not liable for the 1957 deficiency income tax assessed against them individually.

Fourth Issue

The question of whether the 1957 deficiency income tax assessed against Jose Ma. Barcelon for 1957 was ₱4,526.00 or ₱4,306.00, for the purpose of computing the amount of tax credit still due him in the same year, is rendered moot and academic because of the ruling of this Court that the Barcelon brothers and sisters are not subject to deficiency income tax for 1957.

With respect to the amount of ₱122.75 assessed against Emsterio Barcelon, Jr. for 1956, it appearing that the said assessment is not disputed, we take it that said petitioner admits his liability therefor. However, we find that ₱40.00 was included in the said assessment as compromise penalty for non-filing of income tax return. The said amount of compromise penalty should be deducted from ₱122.75, leaving a balance of ₱82.75.

IN VIEW OF THE FOREGOING CONSIDERATIONS, the decision of respondent holding Jose, Teresita, Rosita, Angelita, Luis and Emeterio, Jr., all surnamed Barcelon, liable for 1957 deficiency income tax and interest in the amounts of ₱1,164.66, ₱831.90, ₱600.62, ₱597.08, ₱541.62 and ₱154.40, respectively, is hereby reversed and the said petitioners absolved from the payment thereof. The decision of respondent against Brixton Investment Corporation and Emeterio Barcelon, Jr., relative to their respective income tax liability for 1957 and 1956, is hereby modified. Petitioners Brixton Investment Corporation and Emeterio Barcelon, Jr. are hereby ordered to pay deficiency income tax and interest for 1957 and 1956, in the respective amounts of ₱10,271.90 and ₱82.75, to the Commissioner of Internal Revenue or his duly authorized collection agent. If the deficiency tax is not paid in full within thirty (30) days from the date this decision becomes final and executory, said petitioners shall pay a surcharge of 5% on the unpaid amount of their respective tax liabilities, plus interest thereon at the rate of 1% a month until paid, subject to the limitation on interest prescribed by Section 51 of the National Internal Revenue Code.

SO ORDERED.

Quezon City, April 18, 1967.

Estanislao R. Alvarez
ESTANISLAO R. ALVAREZ
Associate Judge

WE CONCUR:

R. Umali
ROMAN M. UMALI
Presiding Judge

Ramon L. Avanceña
RAMON L. AVANCEÑA
Associate Judge