REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
MANILA

ALHAMBRA CIGAR & CIGARETTE
MANUFACTURING COMPANY,
Petitioner,

- versus - C.T.A. CASE NO. 143

THE COLLECTOR OF INTERNAL
REVENUE,
Respondent.

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

D E C I S I O N

Petitioner Alhambra Cigar and Cigarette Manufacturing Company is a domestic corporation, engaged in the business of manufacturing cigars and cigarettes. For the years 1949, 1950, 1951, 1952 and 1953, it filed its income tax returns on the accrual method of accounting and paid the income taxes computed in accordance therewith. Subsequently, a verfication of petitioner's income tax returns for the said years was conducted by respondent Collector of Internal Revenue, and finding alleged deficiency income taxes due therefrom, assessed and demanded from petitioner the amounts of ₱26,369.04, ₱42,653.00, ₱61,308.00, ₱58,404.00 and ₱51,826.00, respectively, plus 5% surcharge and 1% monthly interest on said amounts commencing on January 15, 1956. Hence, this appeal which was submitted for decision mainly upon a stipulation of facts as follows:

1. That the petitioner herein had filed its income tax returns on the accrual basis and on the following dates:

For the taxable year 1949,	on March 30, 1950;
For the taxable year 1950,	On March 6, 1951;
For the taxable year 1951,	On February 26, 1952;
For the taxable year 1952,	On March 10, 1953; and
For the taxable year 1953,	On February 26, 1954.

2. That the income tax liability of the petitioner for the years 1949 to 1953 had been assessed by the respondent in the amounts as computed and declared by the petitioner in the respective returns as follows:

(a) Assessment No. A-120966,	for 1949 - ₱114,029.80
(b) Assessment No. A-121345,	for 1950 - ₱188,487.00
(c) Assessment No. AC-94-52,	for 1951 - ₱343,240.00
(d) Assessment No. AC-836,	for 1952 - ₱225,503.00
(e) Assessment No. 90-AC-00467	for 1953 - ₱221,937.00

which were all paid by the petitioner in due time.

3. That in a subsequent verification of petitioner's income tax returns for the years 1949 to 1953, inclusive, which was conducted by a representative of respondent, the following deficiency assessments based on the figures declared in the returns, were issued against petitioner on November 27, 1954:

(a) For 1949 - (Assessment No. 90-5C-120966-54-49)	- ₱26,369.04
(b) For 1950 -(Assessment No. 90-5C-121345-54-50)	- ₱42,653.00
(c) For 1951 - (Assessment No. 90-5C-94-54-51)	- ₱61,308.00
(d) For 1952 - (Assessment No. 90-5C-836-54-52)	- ₱58,404.00
(e) For 1953 - (Assessment No. 90-5C-467-54-53)	- ₱51,826.00

4. That the said deficiency income tax assessments for the taxable years 1949, 1950, 1951, 1952 and 1953 were arrived at as follows:

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Net income as per return		₱ 950,248.34
Add: Disallowances:		
Directors' Fees See return	₱90,576.98	
Salary of Kuenzle and Streiff, See return	12,000.00	
Bonus of Kuenzle and Streiff, See return	50,000.00	
Commissions of Kuenzle and Streiff, See return	51,768.94	
Allowance for loss of A. Muñoz Schedule VI	951.92	
Depreciations, Schedules IV and V	2,966.48	
Local Selling Expenses, Schedule III-a	6,088.06	
Charges to Sales Account, Schedule III-b	4,470.84	
Traveling Expenses, Schedule XI	918.79	219,742.01
Total net profit per investigation		₱1,169,990.35
Tax due on the above net income		₱ 140,398.84
Less amount of tax already paid		114,029.80
Deficiency		₱ 26,369.04

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Net income as per return		₱1,178,043.06
Add disallowances:		
Directors' Fees, See return	₱90,854.33	
Salary of Kuenzle and Streiff, See return	12,000.00	
Bonus of Kuenzle and Streiff, See return	50,000.00	

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Commissions of Kuenzle and Streiff, See return	₱54,322.90	
Transportation and Representation, Schedule II	28,100.00	
Repair on Building Schedule VII ...	19,931.00	
Depreciations, Schedules IV and V	2,673.42	
Local Selling Expenses, Schedule III-a	5,635.51	
Charges to Sales Account, Schedule III-b	1,036.15	
Traveling Expenses, Schedule XI	2,029.90	266,583.26
Total net income per investigation		₱1,444,626.32
Tax due thereon		₱ 231,140.00
Less withholding tax already paid		188,487.00
Deficiency		₱ 42,653.00

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Net income as per return		₱1,254,426.82
Add disallowances:		
Directors' Fees, See return	₱71,669.38	
Salary of Kuenzle and Streiff, See return	12,000.00	
Bonus of Kuenzle and Streiff, See return	50,000.00	
Commissions of Kuenzle and Streiff, See return	45,064.62	
Transportation and Representation, Schedule II	27,750.00	
Allowance for loss of Macapagal, Schedule VI	612.37	
Fine, Schedule VI	300.00	
Depreciations,		

Schedules IV and V	₱ 3,719.55	
Local Selling Expenses, Schedule II-a	1,097.61	
Charges to Sales Account, Schedule III-b	3,682.54	
Traveling Expenses, Schedule II	3,063.90	218,959.97
Total net income per investigation		₱1,473,386.97
Tax due thereon		₱ 404,548.00
Less amount of tax paid		343,240.00
Deficiency tax		₱ 61,308.00

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Net income per return		₱ 833,940.99
Add disallowances:		
Directors' Fees,..	₱58,184.11	
Salary of Kuenzle and Streiff	12,000.00	
Bonus of Kuenzle and Streiff	47,500.00	
Commissions of Kuenzle and Streiff	28,894.68	
Transportation and Representation, Schedule II	28,615.14	
Allowance for loss in money counter, Schedule VI	838.00	
Discretionary Expenses, Schedule VI	6,000.00	
Depreciations, Schedules IV and V	2,692.20	
Local Selling Expenses, Schedule III-a	1,145.31	
Charges to Sales Account, Schedule III-b	4,634.70	
Reserve for price fluctuation charged to Purchase Schedule X	18,680.95	208,585.09

Total net income per investigation		₱1,042,526.08
Tax due thereon		₱ 283,907.00
Less amount of tax already paid		225,503.00
Deficiency tax		₱ 58,404.00

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Net income per return		₱ 821,202.51
Add disallowances:		
Directors' Fees ..	₱47,936.60	
Salary of Kuenzle and Streiff	12,000.00	
Bonus of Kuenzle and Streiff	47,500.00	
Commissions of Kuenzle and Streiff	33,992.58	
Transportation and Representation, Schedule II	27,576.54	
Allowance for loss in money counter, Schedule VI	972.00	
Depreciation, Schedule IV	2,167.20	
Local Selling Expenses, Schedule III-a	2,016.98	
Charges to Sales Account, Schedule III-b	4,475.16	
Traveling Expenses, Schedule XI	6,458.83	185,095.89
Total net income per investigation		₱1,006,298.40
Tax due thereon		₱ 273,763.00
Less amount of tax already paid		221,937.00
Deficiency tax		₱ 51,826.00

5. That the petitioner had claimed all the abovementioned disallowed items as deductions in its respective returns.

6. That the said disallowances were based on the respective grounds contained in the report of respondent's Supervising Examiner Gregorio Mendoza, copy of which is Annex "A" of the Petition for Review, and its original, folio 118 of the Bureau of Internal Revenue records of this case, is marked Exhibit "A" for purposes of this stipulation.

7. That the deficiency income tax in question is but a matter of difference of opinion between the petitioner, on one side, and the respondent, on the other side, whether the deductions which were disallowed by the respondent and which are enumerated in paragraph 4 of this stipulation, are deductible or not, and not that the petitioner's income tax returns under consideration are false or fraudulent.

8. That the directors' fees, salaries, bonuses, and commissions paid to Directors A. P. Kuenzle and H. A. Streiff for the taxable years 1949, 1950, 1951, 1952 and 1953 are indicated in the financial statements attached to the petitioner's income tax returns for the said years, as follows:

Name	Directors' Fees	Salary	Bonus	Commission
		1 9 4 9		
A.P. Kuenzle	₱20,585.68	₱6,000.00	₱25,000.00	₱25,884.47
H.A. Streiff	20,585.68	6,000.00	25,000.00	25,884.47
		1 9 5 0		
A.P. Kuenzle	₱20,648.71	₱6,000.00	₱25,000.00	₱27,161.45
H.A. Streiff	20,648.71	6,000.00	25,000.00	27,161.45
		1 9 5 1		
A.P. Kuenzle	₱16,288.43	₱6,000.00	₱25,000.00	₱22,532.31
H.A. Streiff	16,288.43	6,000.00	25,000.00	22,532.31
		1 9 5 2		
A.P. Kuenzle	₱13,223.66	₱6,000.00	₱23,750.00	₱14,447.34
H.A. Streiff	13,223.66	6,000.00	23,750.00	14,447.34
		1 9 5 3		
A.P. Kuenzle	₱10,894.69	₱6,000.00	₱23,750.00	₱16,996.29
H.A. Streiff	10,894.69	6,000.00	23,750.00	16,996.29

9. That the directors' fees paid to directors W. Eggmann, A. Jung, and E. Rupp for the

taxable years 1949,1950, 1951, 1952 and 1953 are indicated in the financial statements attached to the petitioner's income tax returns for the said years, as follows:

DIRECTORS' FEES

	W.Eggmann	A. Jung	E. Rupp	Total
1949	₱16,468.54	₱16,468.54	₱16,468.54	₱49,405.62
1950	16,518.97	16,518.97	16,518.97	49,556.91
1951	13,030.74	13,030.74	13,030.74	39,092.22
1952	10,578.93	10,578.93	10,578.93	31,736.79
1953	8,715.74	8,715.74	8,715.74	26,789.38

10. That, resuming from paragraphs 8 and 9 of this stipulation, the amounts of -

(1) ₱90,576.98 for 1949, ₱90,854.33 for 1950, ₱71,669.38 for 1951, ₱58,184.11 for 1952 and ₱47,936.00 for 1953, as directors' fees which had been disallowed:

(2) ₱12,000.00 for 1949, ₱12,000.00 for 1950, ₱12,000.00 for 1951, ₱12,000.00 for 1952 and ₱12,000.00 for 1953, as salaries of Messrs. Kuenzle and Streiff, which had been disallowed:

(3) ₱50,000.00 for 1949, ₱50,000.00 for 1950, ₱50,000.00 for 1951, ₱47,500.00 for 1952 and ₱47,500.00 for 1953, as bonus of Messrs. Kuenzle and Streiff, which had been disallowed; and

(4) ₱51,768.94 for 1949, ₱54,322.90 for 1950, ₱45,064.62 for 1951, ₱28,894.68 for 1952 and ₱33,992.58 for 1953, as commission of Messrs. Kuenzle and Streiff, which had been disallowed, are respectively made up as follows:

Name	Directors' Fees	Salary	Bonus	Commissions
		1949		
A.P. Kuenzle	₱20,585.68	₱6,000.00	₱25,000.00	₱25,884.47
H.A. Streiff	20,585.68	6,000.00	25,000.00	25,884.47
A. Jung	16,468.54	-.--	-.--	-.--
W. Eggmann	16,468.54	-.--	-.--	-.--
E. Rupp	16,468.54	-.--	-.--	-.--
		1950		
A.P. Kuenzle	₱20,648.71	₱6,000.00	₱25,000.00	₱27,161.45
H.A. Streiff	20,648.71	6,000.00	25,000.00	27,161.45

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A. Jung	₱16,518.97	₱ -.--	₱ -.--	₱ -.--
W. Eggmann	16,518.97	-.--	-.--	-.--
E. Rupp	16,518.97	-.--	-.--	-.--
1 9 5 1				
A.P. Kuenzle	₱16,288.43	₱6,000.00	₱25,000.00	₱22,532.31
H.A. Streiff	16,288.43	6,000.00	25,000.00	22,532.31
A. Jung	13,030.74	-.--	-.--	-.--
W. Eggmann	13,030.74	-.--	-.--	-.--
E. Rupp	13,030.74	-.--	-.--	-.--
1 9 5 2				
A.P. Kuenzle	₱13,223.66	₱6,000.00	₱23,750.00	₱14,447.34
H.A. Streiff	13,223.66	6,000.00	23,750.00	14,447.34
A. Jung	10,578.93	-.--	-.--	-.--
W. Eggmann	10,578.93	-.--	-.--	-.--
E. Rupp	10,578.93	-.--	-.--	-.--
1 9 5 3				
A.P. Kuenzle	₱10,894.69	₱6,000.00	₱23,750.00	₱16,996.29
H.A. Streiff	10,894.69	6,000.00	23,750.00	16,996.29
A. Jung	8,715.74	-.--	-.--	-.--
W. Eggmann	8,715.74	-.--	-.--	-.--
E. Rupp	8,715.74	-.--	-.--	-.--

11. That all of the salaries, bonuses and commissions paid to Directors W. Eggmann, A. Jung and E. Rupp for the taxable years 1949, 1950, 1951, 1952 and 1953 had been allowed by the respondent as deductions (therefore, are not questioned), which are set forth in the financial statements attached to the petitioner's income tax returns for the said years, as follows:

	Salary	Bonus	Commission
	1 9 4 9		
W. Eggmann	₱15,000.00	₱12,000.00	₱25,884.47
A. Jung	-.--	15,500.00	-.--
E. Rupp	12,000.00	12,000.00	-.--
	1 9 5 0		
W. Eggmann	₱15,000.00	₱20,000.00	₱27,161.45
A. Jung	-.--	15,000.00	-.--
E. Rupp	11,600.00	12,000.00	-.--
	1 9 5 1		
W. Eggmann	₱10,375.00	₱17,500.00	₱22,532.31
A. Jung	-.--	13,000.00	-.--
E. Rupp	8,730.00	15,000.00	-.--

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W. Eggmann	₱12,000.00	₱16,650.00	₱14,447.34
A. Jung	-.--	12,350.00	-.--
E. Rupp	9,000.00	14,250.00	-.--

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W. Eggmann	₱12,000.00	₱16,650.00	₱16,996.29
A. Jung	-.--	12,350.00	-.--
E. Rupp	9,000.00	14,250.00	-.--

12. That the said amounts of directors' fees, salary, bonus and commission paid to Mr. A. P. Kuenzle and Mr. H. A. Streiff, for the years 1949 to 1953, inclusive, were disallowed by the respondent on the theory by the respondent that these two individuals were permanently living abroad, as in fact they are.

13. That the petitioner contested the alleged deficiency income taxes assessed by respondent under letter by petitioner's counsel, dated January 14, 1955, appearing in folios 125 to 142 of the Bureau of Internal Revenue records of this case, which is marked as Exhibit "B" for purposes of this stipulation.

14. That the said protest made by the petitioner was denied by the respondent under the latter's letter dated April 21, 1955, appearing in folios 147-148 of the Bureau of Internal Revenue records of the case, which is marked Exhibit "C" for purposes of this stipulation.

15. That due to the refusal of the petitioner to settle the deficiency income taxes in question, under the petitioner's contention that such assessments are erroneous, the respondent issued a warrant of distraint and levy on the property of the petitioner, on April 21, 1955, appearing on folio 149 of the Bureau of Internal Revenue records of this case, which is marked Exhibit "D" for purposes of this stipulation.

16. That by agreement between counsel for both parties, the respondent advised the City Treasurer of the City of Manila to suspend the execution of the warrant of distraint and levy, under his letter dated July 20, 1955, appearing on folio 174 of the Bureau of Internal Revenue records of this case, which is marked Exhibit "E" for purposes of this stipulation.

17. That the disallowed items for "depreciation" for the taxable years 1949 to 1953 consist of the depreciation of autos and trucks as well

as buildings, totalling ₱14,218.85, of which the amount of ₱8,974.66 is the depreciation of the buildings and the amount of ₱5,244.19 is the depreciation of the autos and trucks; and that the petitioner and the respondent hereby agree that, for the years under consideration, the depreciation of the buildings in the aggregate amount of ₱8,974.66 be disallowed and the depreciation of the autos and trucks to be disallowed should be in the aggregate amount of ₱1,646.13. The parties will present at the trial of this case a statement of the breakdown of both amounts indicating the amounts corresponding to each year.

18. That petitioner hereby agree that the fine of ₱300.00 be disallowed.

19. That respondent agrees that deductions for "allowances for loss in money counter" in the amounts of ₱838.00 for 1952 and ₱972.00 for 1953 be allowed.

20. That the parties reserve to themselves the right to submit additional evidence oral as well as documentary.

21. That the officials of the petitioner, who were the recipients of the amounts of ₱28,100.00 for 1950, ₱27,243.33 (not ₱27,750.00 as found by the Bureau of Internal Revenue Examiner Gregorio Mendoza) for 1951, ₱28,756.12 (not ₱28,015.14 as found by the Bureau of Internal Revenue examiner Gregorio Mendoza) for 1952, and ₱28,072.51 (not ₱27,576.54 as found by the Bureau of Internal Revenue examiner Gregorio Mendoza) for 1953, for "transportation and representation", and the position they respectively held and the amounts paid to them individually are as follows:

Name	Position Held	1950	1951	1952	1953
Bogo, D.	Supervisor Valley Branch	₱ -.--	₱ -.--	₱ -.--	₱ 687.10
Eggmann, W.	General Manager	3,000.00	3,000.00	3,000.00	3,000.00
Fernandez, M.	Sales Supervisor	2,400.00	2,400.00	831.15	-.--
Ferrandiz, M.	Factory Supervisor	2,400.00	2,400.00	2,400.00	1,292.05
Garcia, R.	Factory Supervisor	1,200.00	1,000.00	900.00	1,200.00
Huber, J.	Asst. Manager, Valley Branch	1,200.00	28.33	613.01	2,000.00

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Koller, F.	Sales Manager	₱ 3,000.00	₱ 3,000.00	₱ 3,000.00	₱3,000.00
Redinger, C.	Chief, Engineer	3,000.00	3,000.00	3,000.00	3,000.00
Ramp, W.	Supervisor, Valley Branch	500.00	500.00	-.--	-.--
Reupke, J.	Factory Superintendent	3,000.00	3,000.00	3,000.00	2,704.11
Rupp, E.	Manager, Valley Branch	3,000.00	-.--	-.--	-.--
Schmid, H.	Asst. Accountant	-.--	-.--	-.--	685.48
Roeder, R.	Asst. Engineer	-.--	-.--	970.98	500.00
Streuli, P.	Supervisor, Valley Branch	1,200.00	1,000.00	1,200.00	328.77
Sulzer, H.	Chief-Accountant	3,000.00	3,000.00	3,000.00	3,000.00
Teucher, W.	Factory Accountant	-.--	3,000.00	3,000.00	3,000.00
Tomelden, B.	Auditor	-.--	675.00	900.00	675.00
Wehrli, G.	Asst. Sales Manager	1,200.00	1,240.00	2,940.98	3,000.00
	T O T A L -	₱28,100.00	₱27,243.33	₱28,756.12	₱28,072.51
	TOTAL, as per B.I.R. -	₱28,100.00	₱27,750.00	₱28,015.14	₱27,576.54
	Difference -	₱ -.--	(₱ 506.67)	₱ 740.98	₱ 495.97

22. That the total amounts declared by the petitioner as deductions, for "traveling expenses", actually paid to its officials and other employees were: ₱9,987.02 for 1949, ₱11,365.54 for 1950, ₱11,695.58 for 1951, ₱5,293.60 for 1952 and ₱16,998.45 for 1953; of which amounts the following traveling expenses were allowed and disallowed, as deductions:

Beneficiary	Total Amount Claimed	Allowed	Disallowed
	1 9 4 9		
Mrs. J. Reupke (For passage to United States)	₱ 918.79	None	₱ 918.79

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Mr. and Mrs. H. Sulzer (For passage to Europe and return)	₱3,751.00	₱1,875.50	₱1,875.50
Mr. and Mrs. H Sulzer (For additional payment for passage from Europe to Manila)	308.80	154.40	154.40

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Mr. and Mrs. W. Eggmann and child (For passage to Europe and return)	₱5,106.50	₱2,042.60	₱3,063.90

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Mr. and Mrs. M Ferrandiz (For passage to Europe and return)	₱4,897.20	₱2,448.60	₱2,448.60
Mr. and Mrs. J. Reupke (For passage to Europe and return)	₱4,939.20	₱2,469.60	₱2,469.60
Mr. and Mrs. H. A. Streiff (One-half of cost of passage from Europe to Manila and to Europe)	₱3,079.65	₱1,539.82	₱1,539.83

23. That the amount of ₱8,974.66, representing depreciation of buildings, which the petitioner and the respondent have agreed to be disallowed, subject matter of paragraph 17 of this stipulation, is broken down in respect to the years they correspond as follows:

For 1949 -------	₱1,543.42
For 1950 -------	1,548.42
For 1951 -------	1,548.42
For 1952 -------	2,167.20
For 1953 -------	2,167.20
	₱8,974.66

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> The amount of ₱1,646.12 representing depreciation of autos and trucks, which the petitioner and the respondent have agreed to be disallowed, also subject matter of paragraph 17 of this stipulation, corresponds to 1951.

As stated elsewhere in the stipulation of facts, simultaneous with the filing of the petition for review, petitioner filed a motion to restrain respondent and/or his representatives from executing, or causing the execution of, the warrant of distraint and levy issued by the latter on April 21, 1955, for the collection of the alleged deficiency income taxes in question. However, by agreement of the parties, respondent suspended the execution of the said warrant of distraint and levy. The first question, therefore, is whether or not respondent's right to collect through summary administrative methods the alleged deficiency income taxes for the years 1949 to 1953, inclusive, has already prescribed.

There is no dispute that the income tax returns of petitioner for the years in question were filed on the following dates:

For the taxable year 1949 - - - March 30, 1950

For the taxable year 1950 - - - March 6, 1951

For the taxable year 1951 - - - February 26, 1952

For the taxable year 1952 - - - March 10, 1953

For the taxable year 1953 - - - February 26, 1954.

Under Section 51 (d) of the National Internal Revenue Code, in cases of erroneous, false or fraudulent returns, the Collector of Internal Revenue shall, upon the discovery thereof, at any time within three years

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after said return is due, or has been made, make a return upon information obtained as provided for in the said code or by existing law, or require the necessary corrections to be made, and the assessment made by him thereon shall be paid by such person or corporation immediately upon notification of the amount of such assessment. The established jurisprudence under this provision of law is that after three years have elapsed from the date on which income tax returns which have been found to be false, fraudulent or erroneous may have been made, the Collector of Internal Revenue cannot make any summary collection thru administrative methods but must do so thru judicial proceedings. (See Collector of Internal Venue v. Villegas, 56 Phil. 554; Collector of Internal Revenue v. Haygood, 65 Phil. 520; Philippine Sugar Development Co. v. Posadas, 68 Phil. 216). This doctrine has been consistently followed and applied by this Court in several cases, among which are, Jose Zulueta v. Collector of Internal Revenue, C.T.A. Case No. 62; Jose Yulo v. J. Antonio Araneta, C.T.A. Case No. 84; Carmen Cuenco vs. Collector of Internal Revenue, C.T.A. Case No. 113; and William Li Yao v. Collector of Internal Revenue, C.T.A. Case No. 30. As the warrant of distraint and levy was issued on April 21, 1955 on the property of petitioner, it follows that respondent can no longer collect the alleged deficiency income taxes of the former for the taxable years 1949, 1950 and 1951, through summary administrative proceedings.

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This brings us to the principal question involved in this case, as raised by the pleadings and as elucidated in the stipulation of facts, whether or not the disallowance by respondent of the items mentioned therein claimed by petitioner as deductions in its income tax returns for the years 1949 to 1953, inclusive, is legally justified.

At the outset, it will be noted that most of the items in question involve expenses claimed by petitioner as incurred in carrying on its business and therefore allowable as deductions for income tax purposes. Under the provisions of Section 30 (a) (1) of the National Internal Revenue Code, a taxpayer is not allowed to claim expenses as deductions unless the same are ordinary and necessary in the maintenance and operation of his trade or business. These include a reasonable allowance for salaries or other compensation for personal services actually rendered and traveling expenses while away from home in the pursuit of a trade or business. And in a suit for the allowance of items representing business expenses, the burden of establishing that the same are ordinary and necessary rest upon him in order to show that he is entitled to the deductions which the Collector of Internal Revenue has disallowed.

> "The allowance of deductions is a matter of legislative grace and the burden is upon the taxpayer to show that the statute sanctions the deduction claimed." (Woolford Realty Co. v. Rose, 286 U.S. 319; Brown v. Helvering, 291 U.S. 193; New Colonial Ice Co. v. Helvering, 292 U.S. 435; McDonald v. Comm., 323 U.S. 51)

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Consequently, for purposes of determining taxable net income , deductions will have to be limited to amounts which, in accordance with the evidence presented, are no more than ordinary and necessary expenses of carrying on the business.

In the light of the above, we shall now discuss the different disputed items ad seriatim.

1. Directors' Fees, Salaries, Bonuses and Commissions of Kuenzle and Streiff for 1949 to 1953, inclusive, shown and indicated under paragraph 8 of the Stipulation of Facts. - A. P. Kuenzle and Harry A. Streiff are the non-resident president and vice-president, respectively, of petitioner, a resident corporation organized and existing under the laws of the Philippines. They are also directors and stockholders of petitioner, owning, together with their families, practically all the shares of stock. In accordance with the by-laws of the corporation they are supposed to perform all duties pertaining to the general supervision of the officers. In view of their permanent absence from the Philippines, however, they perform only those duties, which, by their nature, could be done by means of directives. Consequently, their actual services are largely limited to the statement of the general policies of petitioner without executive supervision and functional control over the implementation of such policies and without any means of checking whether the same are put into proper operation. While regular correspondence is maintained between them and petitioner, they act only on matters that

are brought to their personal attention.

It follows that the evidence before us supports the conclusion that personal services actually rendered by A. P. Kuenzle and Harry. A. Streiff are not as worthless as determined by respondent. A reasonable allowance therefor, however, would not, in our opinion, exceed ₱6,000.00 per annum each as has been determined by petitioner and a bonus not to exceed the amount of their respective salary.

We do not have here any evidence regarding the nature, extent or value of the services of A. P. Kuenzle and Harry A. Streiff so as to entitle them to further compensation in forms of commissions. Neither is there any showing as to the basis of apportionment of such commissions, whether the nature and extent of their services, the amount of their stockholdings, the value of their services, or otherwise. While this Court should be slow to reject the determination of a corporation as to the reasonableness of the salaries of its employees, petitioner has not presented any proof that a correct determination would exceed that of respondent. Since the amounts of commissions given to A. P. Kuenzle and Harry A. Streiff do not comport with the statutory qualifications of tax deductions, same are therefore disallowed as determined by respondent.

The same is true with regards to the directors' fees paid to A. P. Kuenzle and Harry A. Streiff during the years in question. The record of the case does not show the nature or extent of the services rendered by the board of directors or the individual members thereof, the basis of apportionment, the value of their services, or the reasonableness of the purported directors' fees. Neither is there any showing that A. P. Kuenzle or Harry A. Streiff presided over or even attended any of the meetings of the board of directors and/or of the stockholders. In fact, nowhere and in no wise does the record show of any meeting of the board of directors during all the years 1949, 1950, 1951, 1952 and 1953.

We believe we do not find it necessary to determine here whether the amounts allegedly representing directors' fees paid by petitioner to these officers as compensation for their services as directors cannot be allowed as ordinary and necessary expenses within the purview of Section 30(a)(1) of the National Internal Revenue Code. However, suffice it to say that these extraordinary and unusual amounts paid by petitioner to these directors in the guise and form of compensation for their supposed services as such, without any relation to the measure of their actual services, cannot be regarded as ordinary and necessary expenses within the meaning of the law. While petitioner argues that as president and vice-president, respectively, the entire salaries, bonuses, commissions and directors' fees paid to A. P. Kuenzle and Harry A. Streiff represent compensation for services actually rendered, it should be noted that for purposes of determining taxable net income, deductions are limited to amounts which are reasonably commensurate with the personal services actually rendered. And in view of the circumstance that these individuals practically own all the shares of stock of the corporation, we would require more convincing proof of the reasonableness of their purported compensation and that proof must also show that such alleged salaries, bonuses, commissions and directors' fees are not disguised distributions of profits.

The pretension has heretofore been made that the fact that the operations of petitioner during the years in question have resulted in substantial gains, as shown by the income tax returns of the corporation for said years, is eloquent proof that the policies laid down by A. P. Kuenzle and H. A. Streiff have been of great benefit to petitioner. While it might superficially appear that the total compensation paid to these non-resident executives, who practically own all of the shares of stock of petitioner, is reasonable in proportion to corporate earnings, it does not appear that these amounts given to them as compensation are reasonable in comparison to their actual services. To test salary deductions alone by determining the ratio of the total compensation of two non-resident officers, owning practically all the shares of stock, in proportion to earnings, would result in the disregard of the statutory requirement of substantial relation between individual service and the compensation therefor, and the recognition of a mathematical gross maximum for two individuals who are in a position to dictate, by reason of proprietary and official considerations, the fixing of their corporate salaries. There is no evidence of the prevailing salaries, bonuses, commissions and other fees paid to employees actually and personally performing similar services in comparable enterprises, the availability or non-availability of others to fill the offices held by them and the salary policy of petitioner as to all its employees. Neither is there evidence of how much petitioner would have to pay to get others to do what A. P. Kuenzle and H. A. Streiff did. Nevertheless, the record of the case shows that there were services performed by them and as best, we determined the deduction indicated by the evidence.

2. Directors' Fees paid to W. Eggmann, A. Jung and E. Rupp for the years 1949, 1950, 1951, 1952 and 1953, as shown and indicated in paragraph 9 of the Stipulation of Facts:- Petitioner deducted these amounts among its business expenses but respondent disallowed them on the ground that the election of W. Eggmann, A. Jung and E. Rupp to the board of directors was null and void per se. After petitioner has presented its evidence to prove that the ground relied upon by respondent for the disallowance of the directors' fees has no basis in law or in fact, the latter, however, admitted in his memorandum that W. Eggmann, A. Jung and E. Rupp are members of the board of directors but argues for the first time for the disallowance of these deduction on the ground that petitioner has not sustained the burden of showing that these individuals have rendered actual services commensurate to their fees as directors. In our opinion, the argument must fail.

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Without in the least attempting to express an opinion whether these amounts exceeded those which, as a matter of common knowledge, are usually paid to directors for the discharge of their customary duties, we believe that, after the case has already been submitted for decision, respondent cannot anymore change his stand and raise for the first time in his memorandum the question as to whether or not W. Eggmann, A. Jung and E. Rupp have rendered actual services as directors of the corporation. Otherwise, if we are to permit respondent to switch from one view to another whenever his convenience suits him, and at this stage of the proceedings after he has already admitted of the weakness of his ground, would be tantamount to allowing him to place taxpayers in a position where, in the prosecution of their tax cases, there would be nothing to guide them but the whims and caprices of his subordinate officers. Respondent relies upon the theory that his assessment is prima facie correct unless controverted, but having predicated the disallowance of the directors' fees in question solely on his belief that the election of the recipients as directors is null and void per se, we believe he cannot now successfully insist that the same should also be disallowed on the alleged ground that petitioner has not established that W. Eggmann, A. Jung and E. Rupp did not render services reasonably commensurate with their compensation. More so, after he had already admitted that the basis of his assessment is ground-less and at a stage of the proceedings where petitioner cannot anymore defend itself. The amounts paid as directors' fees to W. Eggmann, A. Jung and E. Rupp for the years in question and disallowed by respondent should therefore be allowed.

3. Local Selling Expenses:- The next disputed item a.
refers to the selling expenses from 1949 to 1953, inclusive, involving an aggregate amount of ₱15,983.47 broken down as follows: 1949-₱6,088.06, 1950-₱5,635.51, 1951-₱1,097.61, 1952-₱1,145.31 and 1953-₱2,016.98. Respondent disallowed this item on the ground that at the end of every semester, the same is debited to this account and credited to accounts payable with the explanation "Salesman Liquidation." Inasmuch as the credits to accounts payable do not represent specific liabilities but in the nature of reserves, respondent maintains that they are not allowable deductions.

The record shows, thru the testimony of Mr. W. Eggmann, that these disputed amounts are not reserves but expenses actually incurred by petitioner's salesmen paid to them and made to accrue as of the end of the year in conformity with sound accounting principles to match income earned with expenses incurred. It appearing that the expenses in question are actual business expenses which form part of the normal selling costs, consequently, they are deductible from the gross income for income tax purposes.

4. Transportation and Representation Allowances:- a in part
The recipients of the transportation and representation

allowances, who are all members of the staff of petitioner, the position they respectively held and the amounts paid to them individually are set forth in paragraph 21 of the stipulation of facts. Petitioner contends that since the allowances in question have been actually disbursed and received by the respective recipient, it has already incurred a business expense deductible under the income tax law. On the other hand, respondent maintains, after petitioner has presented its evidence, that in the cases of C. Reginger, B. Tomelden, M. Fernandez, R. Garcia, J. Reupke, H. Schmid, R. Roeder, H. Sulzer and W. Teucher, the nature of their work is such that their positions do not require traveling or representation expenses. While he argues that the expenses claimed for these individuals are not reasonable nor necessary in the pursuit of the business of the corporation and consequently are not deductible, respondent does not question anymore the reasonableness and necessity of the expenses of the other recipients. With regard to D. Bogo, W. Eggmann, M. Ferrandiz, J. Huber, F. Koller, W. Ramp, E. Rupp, P. Streuli and G. Wehrli, we shall therefore consider that respondent is satisfied that the two requirements of the law of "ordinary and necessary" and "trade or business" have been duly fulfilled. It follows that their respective transportation and representation allowances, as shown in paragraph 21 of the stipulation of facts, are deductible. Hence, the following discussion will be limited to those employees whose trans-

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portation and representation allowances are disputed by respondent.

As already stated above, even if the expense is incurred in carrying on a trade or business, it must also be an ordinary and necessary expense proximately related to the trade or business. "Necessary" may mean merely "appropriate" or "helpful" to the business; but "ordinary" connotes a payment which is normal in relation to the business of the taxpayer and the circumstances. (See Deputy v. du Pont, 308 U.S. 488).

Now, how appropriate and helpful were the expenditures in question in the operation or maintenance of petitioner's business? While this Court should be slow to override the judgment of petitioner which led to these payments, as such payments may be assumed to have been required by its business, the record of the case is silent as to the motivations and requirements which prompted petitioner to conclude that such disbursements were necessary to the conduct of its business. Neither is there any evidence that the transportation and representation allowances in question have some reasonably normal relation to the ordinary conduct of petitioner's business and the circumstances surrounding their payments. We believe that expenses are not deductible merely because they are incurred in connection with the business of the taxpayer. As the law requires, the payments must also constitute necessary and ordinary expenses of carrying on the business. Since petitioner has not sustained the burden of showing that the transportation and representation allowances paid to C. Reginger, B. Tomelden, M. Fernandez, R. Garcia, J. Reupke, H. Schmid, R. Roeder, H. Sulzer and W. Teucher during the years in question were in fact part of its ordinary and necessary expenses, same must, for this reason, be disallowed.

5. Charges to Sales Account:- This item refers to "charges to sales account" from 1949 to 1953, inclusive, representing a total amount of ₱18,299.39 broken as follows: 1949-₱4,470.84, 1950-₱1,036.15, 1951-₱3,682.54, 1952-₱4,634.70 and 1953-₱4,475.16. Respondent disallowed this item on the ground that the amounts represented by it, are in the nature of reserves like charges to selling expenses and are not actual expenses incurred. In like manner, the testimony of Mr. W. Eggmann in this regard, which was never contradicted, is to the effect that these amounts represent accrual of turnover discounts to petitioner's wholesale customers pertaining to sales made during the year but only paid at the close of the calendar year. Such being the case, and it appearing that they were not disallowed by respondent because they are not ordinary and necessary expenses of carrying on the business of petitioner, we believe that they are deductible for purposes of determining taxable net income.

6. Depreciation (1949 to 1953, inclusive:- The parties have agreed that the disallowed items for depreciation for the years in question consist of the depreciation of autos and trucks, as well as buildings,

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totalling ₱14,218.85, of which the amount of ₱8,974.66 is the depreciation of the buildings and the sum of ₱5,244.19 is the depreciation of the autos and trucks. Both parties have also agreed that the depreciation of the buildings in the said amount of ₱8,974.66 is to be disallowed and the depreciation of the autos and trucks to be disallowed should be in the sum of ₱1,646.13. (par. 17, Stipulation of Facts). The breakdown of the amount of ₱8,974.66 in respect to the years they correspond is as follows: 1949-₱1,543.42, 1950-₱1,548.42, 1951-₱1,548.42, 1952-₱2,167.20 and 1953-₱2,167.20. The amount of ₱1,646.12 representing depreciation of autos and trucks corresponds to 1951. (par. 23, Stipulation of Facts). We shall consider these amounts in the computation of the entire taxes.

7. Allowances for losses of Muñoz (for 1949 only), Macapagal (for 1951 only) money counter (for 1952 and 1953 only), and fine:- With respect to the "allowances for losses in money counter" in the amounts of ₱838.00 for 1952 and ₱972.00 for 1953, respondent has agreed not to question the deductibility of the same. (par. 19, Stipulation of Facts). The petitioner has agreed also that the item on fine amounting to ₱300.00 be disallowed. It is therefore unnecessary to pass upon these items.

Anent the allowance for loss of funds in the custody of Macapagal in 1951, the amount involved is ₱612.37 as shown by paragraph 5 of the petition for review and paragraph 4 of the stipulation of facts.

While petitioner claims that the amount involved is only ₱281.37, there being no proof presented to this effect, the sum stated in the stipulation of facts should govern~~ed~~. Respondent contends that this amount is not a deductible item because it can be paid or compensated by the employee concerned. On the other hand, petitioner insists that it is a deductible item for it was not actually recovered from the employee.

It has already been held that the deduction for losses is forfeited to the extent that the taxpayer could have mitigated his loss. In the case of Messenger Corp. v. Smith, 136 F (2d) 172, the taxpayer had failed to file a claim against its bankrupt debtor, because the estate was believed to be too small to warrant the action. The loss was denied to the extent that recovery could have been had. For tax purposes, the court held, the taxpayer was under duty to file its claim. Without trying to express an opinion whether the potential recovery factor carries with it an action in court, in the instant case, petitioner has not shown of any step or steps which it had taken to recover or even mitigate the loss. And more so, when the person concerned is its own employee.

With regards to the allowance for the loss of Muñoz for 1949, it appears that Muñoz was petitioner's salesman stationed in San Fernando, Pampanga. He made a sale on credit in Angeles and later on sent his driver to collect the money. His driver was held up and robbed of his collection amounting to ₱1,903.04. This occurred sometime in November of 1948, but petitioner's management had the matter investigated only in the early part of 1949. After it was satisfied that Muñoz or his driver could not be entirely blamed for such loss, petitioner bore one-half of the sum of ₱1,903.04, or ₱951.92, and the other half was paid by Muñoz. The deductibility of the said amount of ₱951.92 borne by the corporation is now the point in controversy between the parties.

Respondent contends that the responsible employee should be the one to shoulder the burden and not the corporation; and if ever the loss should be allowed, it should have been claimed in 1948, not in 1949. Petitioner claims otherwise.

Under the circumstances surrounding the disappearance of the money in question, petitioner took every step to mitigate, if not to recover, its loss. While it does not appear that an action was brought for the recovery thereof, an investigation was conducted by petitioner and the facts brought out therein were such that the salesman was not entirely to be blamed. Respondent admits that the loss resulted from robbery, and although the liability of the salesman was found by the corporation to be doubtful, petitioner was able to reduce its loss by one-half. And on the contention of respondent that the loss should have been claimed in 1948, it will be noted that the law contemplates the deduction from gross income of losses only which are fixed by identifiable events. The income tax law is concerned only with realized losses and it was only in 1949 that petitioner reasonably ascertained the fact of and the amount of the loss so as to justify its deduction. Before that, the loss was not yet evidenced by a closed and completed transaction as the possibility of reimbursement was still real and substantial. The said amount of ₱951.92 is therefore an allowable deduction in 1949.

8. Traveling Expenses:- The total amounts declared and claimed by petitioner as deductions for traveling expenses paid to its officials and employees, together with their families, were ₱9,987.02 for 1949, ₱11,365.54 for 1950, ₱11,695.58 for 1951, ₱5,293.60 for 1952 and ₱16,998.45 for 1953. (par. 22, Stipulation of Facts). All these total amounts were claimed by petitioner as business expenses, but respondent disallowed ₱918.79 for 1949, ₱2,029.90 for 1950, ₱3,063.90 for 1951 and ₱6,458.83 for 1953, on the ground that they are personal in nature, having been incurred as traveling expenses of the wives of certain employees of the corporation.

As correctly stated by petitioner in its memorandum, the amounts in question represent additional compensation paid by the corporation to the recipients thereof. Hence, the allowance of these deductions from gross income does not turn on whether they were incurred in the pursuit of a trade or business while away from home, but depends on whether they constitute ordinary and necessary expenses paid or incurred in carrying on the business of petitioner.

It is already well-settled that even though payment is intended to be and is compensation for services rendered, only such part thereof may be deducted as represents reasonable compensation under all the circumstances. It is also well-established that the burden of proof of reasonableness is on the taxpayer, and a claim for salary deduction will be disallowed unless its reasonableness is proved. Thus, amounts paid by a corporation to its officers having no substantial relation to the measure of their services and disproportionate to their value, are not in reality payment for services, and cannot be regarded as "ordinary and necessary expenses" within the meaning of the law; and that such amounts do not become part of the "ordinary and necessary expenses" merely because the payments are made in accordance with an agreement between the corporation and its officers. Even if binding upon the parties, such an agreement does not change the character of the purported compensation or constitute it, as against the government, an ordinary and necessary expense. (See Botany Worsted Mills v. U.S., 278 U.S. 282, 73 L. Ed. 379, 49 S. Ct. 129 (1929).

In the light of the above, does the record of the case show whether the amounts disallowed by respondent constitute ordinary and necessary expenses paid or incurred by petitioner in carrying on its business? While it is true that there is no fixed yardstick by which the question of the reasonableness of the compensation in any particular case can be measured, petitioner has not presented any evidence from which this Court can make the necessary inference that the amounts disallowed by respondent were in fact parts of its ordinary and necessary expenses. The evidence for petitioner shows that the employment contracts between the corporation and the recipients of the traveling expenses in question, who are foreigners, provide that the latter are entitled to transportation expenses to the Philippines for themselves and their families, and also for home leave to their respective countries after every few years in this country, with the traveling expenses for themselves and their families paid by the corporation, but as stated above, such an agreement does not change the character of the purported compensation or constitute it, as against the government, an ordinary and necessary expense. The amounts claimed by petitioner as deductions for traveling expenses under this item must, for this reason, be therefore disallowed.

9. Repair of Building, 1950:- This item refers to the sum of ₱19,931.05 representing expenses for the construction of a new fence around a certain part of petitioner's factory compound in Manila, which respondent contends as chargeable to capital expenditures. Petitioner charged off the entire amount as expense during the year in which it was incurred, instead of charging it to capital expenditures and depreciating its value.

In determining whether an expenditure is a capital one or is chargeable against operating income, it is necessary to bear in mind the purpose for which the expenditure was made. To repair is to restore to a sound state or to mend, while a replacement connotes a substitution. A repair is an expenditure for the purpose of keeping the property in an ordinarily efficient operating condition. It does not add to the value of the property, nor does it appreciably prolong its life. It merely keeps the property in an operating condition over its probable useful life for the uses for which it was acquired. Expenditures for that purpose are distinguishable from those for replacements, alterations, improvements or additions which prolong the life of the property, increase its value, or make it adaptable to a different use. The one is a maintenance charge, while the others are additions to capital investment which should not be applied against current earnings. (See Illinois Merchants Trust Co., Executor, 4 BTA 103; J. Bently Squier, 13 BTA 1225)

> Theoretically, the expenses chargeable to earnings include the general expenses of keeping up the organization of the company, and all expenses incurred in operating the works and keeping them in good condition and repair; whilst expenses chargeable to capital include those which are incurred in the original construction of the works, and in the subsequent enlargement and improvement thereof. (Union Pacific R. R. Co. v. United States, 99 U.S. 402).

Applying these principles to the facts of the case, there is no question that by this expenditure, there was an original construction of a hallow block fence with iron grills around the compound occupied by petitioner and in the subsequent improvement thereof. The record of the case is clear that the amount in question did not merely involve the cost of incidental repairs for the purpose of keeping the property of the corporation in an ordinarily efficient operating condition, but an addition which prolonged the life of such property and which materially increased its value. It was not just a maintenance charge or an expense of keeping up the business of petitioner. We are therefore of the opinion that the sum of ₱19,931.05 referred to under this item is a capital expenditure which should not be applied against current earnings.

10. Discretionary Expenses of Mr. Eggmann for 1952:- Mr. Eggmann is the treasurer and acting manager of petitioner and in 1952, he was given the sum of ₱6,000.00 to be spent as in his judgment will redound to the benefit and interest of the corporation. It appears that the said amount was spent by him in so many little items that it would be very difficult to classify them. While petitioner claims that it was actually spent for such purpose, respondent however disallowed the same on the ground that the former failed to prove that the expenditure constitute an ordinary and necessary business expense of the corporation. In our opinion, the argument should be sustained.

The giving of discretionary funds to top executives of business enterprises is a common practice in any industry. However, since in most instances there is a large personal element involved, the necessity of such expenditures or the direct business benefits to be derived therefrom is a prerequisite to the allowance of the same as deductible expense. These expenses must be not only necessary but also ordinary within the accepted and known meanings of these two terms. And the fact that the taxpayer thinks that the expense is a proper deduction will not control because to be deductible, it must meet the test laid down by the income tax law.

Without in the least attempting to belittle Mr. Eggmann's judgment as to the necessity of such expenditures because of the substantial difference in opinion as to their value, it will be noticed that petitioner failed to prove the direct business benefits which reasonably stemmed from the expenditure of the discretionary fund in question. Petitioner claims that the said amount was spent in connection with its business, but no evidence to this effect was presented by it. It needs hardly necessary to add that to be deductible, these expenses must be both ordinary and necessary and incurred in carrying on the business of the corporation, and the burden of proof is upon petitioner to show the definite reasonable business purpose behind such expenditures and that the same were reasonably calculated to accomplish that purpose. We are not unmindful of the fact that, perhaps, because the results flowing from these expenditures are more or less intangible in nature, it may sometimes be difficult to prove that the payments constituted ordinary and necessary business expenses, but the record of the case shows that there was not even a substantial compliance with the requirements of the law. For this reason, the amount of ₱6,000.00 representing discretionary expenses of Mr. Eggmann for 1952 should therefore be disallowed.

11. Reserve for Price Fluctuation for 1952:- The last disputed item refers to reserve for price fluctuation for 1952, which involved the sum of ₱18,680.95. The disallowance of this item by respondent is based on the general proposition that amounts deposited in a reserve to cover contingent liabilities cannot be deducted until such liabilities become fixed.

It appears that in 1950, petitioner created a "Reserve for Price Fluctuation" but such reserve was not claimed as a deduction for that year, since no loss chargeable to this account was actually sustained. In 1952 the corporation sustained an actual loss on a sale of raw leaf tobacco and such loss was chargeable in that year against this reserve which was created for the purpose in 1951. Clearly therefore, the amount in question represented loss actually sustained by petitioner in 1952 and is in conformity with the theory of respondent that if the price really fluctuates, the loss will be deducted in the year it is sustained. Petitioner having claimed the deduction in question for 1952, the year when the loss was actually sustained, and not for 1951 when the reserve was created, the amount of ₱18,680.95 should therefore be allowed.

From the foregoing, we are therefore of the opinion and so hold that: (1) the directors' fees and commissions of A. P. Kuenzle and H. A. Streiff for 1949 to 1953, inclusive, as itemized in paragraph 8 of the stipulation of facts, are totally disallowed but their entire salaries and yearly bonuses not to exceed the amount of their respective salary rate are allowed; (2) the entire directors' fees of W. Eggmann, A. Jung and E. Rupp for the years 1949, 1950, 1951, 1952 and 1953, as indicated in paragraph 9 of the stipulation of facts, are considered as allowable deductions; (3) the local selling expenses of petitioner from 1949 to 1953, inclusive, involving an aggregate sum of ₱15,983.47, appearing in paragraph 4 of the stipulation of facts, are deductible from the gross income; (4) the transportation and representation allowances paid to C. Reginger, B. Tomelden, M. Fernandez, R. Garcia, J. Reupke, H. Schmid, R. Roeder, H. Sulzer and W. Teucher during the years 1950, 1951, 1952 and 1953, as set forth in paragraph 21 of the stipulation of facts, are disallowed, while those of D. Bogo, W. Eggmann, M. Ferrandiz, J. Huber, F. Koller, W. Ramp, E. Rupp, P. Streuli and G. Wehrli are allowed; (5) the charges to sales account from 1949 to 1953, inclusive, representing a total amount of ₱18,299.39, as shown in paragraph 4 of the stipulation of facts, are deductible; (6) the depreciation of building and that of the autos and trucks to be disallowed are the sums of ₱8,974.66 and ₱1,646.13, respectively, which are broken down in respect to the years they correspond in paragraph 23 of the stipulation of facts; (7) the allowances for losses in the money counter in the amounts of ₱838.00 for 1952 and ₱972.00 for 1953 are allowed, although the fine of ₱300.00 is disallowed, and with regards to the allowance for loss of funds in the custody of Macapagal in 1951 in the sum of ₱612.37, same is not deductible while that of Muñoz for 1949 in the amount of ₱951.92 is an allowable deduction; (8) the amounts of ₱918.79 for 1949, ₱2,029.90 for 1950, ₱3,063.90 for 1951 and ₱6,458.83 for 1953 representing traveling expenses disallowed by respondent are not allowable deductions; (9) the sum of ₱19,931.05 representing expenses for the construction of a new fence around petitioner's compound is a capital expenditure so that it cannot be charged off as expense in 1950; (10) the discretionary expenses of Mr. Eggmann for 1952 in the amount of ₱6,000.00 is disallowed; and (11) the reserve for price fluctuation for 1952 in the amount of ₱18,680.95 is allowed.

WHEREFORE, the appealed decision is hereby modified in the sense that petitioner Alhambra Cigar & Cigarette Manufacturing Company should pay respondent Collector of Internal Revenue the sums of ₱16,008.30, ₱27,157.00, ₱38,888.00, ₱32,092.00, and ₱32,108.00, representing deficiency income taxes for the years 1949, 1950, 1951, 1952 and 1953, respectively, or a total of ₱146,253.30, computed as follows:

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Net Income as per return		₱ 950.248.34
Add disallowances:		
Directors' fees	₱ 41,171.36	
Bonus of Kuenzle and Streiff	38,000.00	
Commissions of Kuenzle & Streiff	51,768.94	
Depreciation of buildings	1,543.42	
Traveling Expenses	(918.79)	133,402.51
Total Net Income		₱1,083,650.85
Tax due on above		₱ 130,038.10
Tax already paid		114,029.80
Deficiency		₱ 16,008.30

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Net Income as per return		₱1,178,043.06
Add disallowances		
Directors' Fees	₱ 41,297.42	
Bonus of Kuenzle and Streiff	38,000.00	
Commissions of Kuenzle & Streiff	54,322.90	
Depreciation of buildings	1,548.42	
Traveling Expenses	(2,029.90)	
Transportation and representation expenses	(12,600.00)	
Repair on buildings	19,931.05	169,729.69
Total Net Income		₱1,347,772.75
Tax due on above		₱ 215,644.00
Tax already paid		188,487.00
Deficiency		₱ 27,157.00

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Net Income as per return		₱1,254,426.82
Add disallowances:		
Directors' fees	₱ 32,576.86	
Bonus of Kuenzle and Streiff	38,000.00	

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Commissions of Kuenzle & Streiff	₱ 45,064.62		
Allowances for loss of Macapagal	~~612.37~~		281.37
Depreciation of buildings	1,548.42		
Depreciation of autos and trucks	1,646.12		
Traveling Expenses	(3,063.90)		
Transportation and representation expenses	(16,075.00)		
Fine	300.00	₱ 138,887.29	
Total Net Income		₱1,393,314.11	
Tax due on above		₱ 382,128.00	
Tax already paid		343,240.00	
Deficiency		₱ 38,888.00	

1 9 5 2

Net Income as per return		₱ 833.940.99	
Add disallowances:			
Directors' fees	₱ 26,447.32		
Bonus for Kuenzle and Streiff	35,500.00		(21,300-)
Commissions for Kuenzle & Streiff	28,894.68		
Depreciation of buildings	2,167.20		
Transportation and representation expenses	(15,602.13)		
Discretionary expenses	6,000.00	114,611.33	
Total Net Income		₱ 948,552.32	
Tax due on above		₱ 257,595.00	
Tax already paid		225,503.00	
Defidiency		₱ 32,092.00	

1 9 5 3

Net Income as per return		₱ 821,202.51	
Add disallowances:			
Directors' fees	₱ 21,789.38		
Bonus of Kuenzle and Streiff	35,500.00		(21,300-)
Commissions of Kuenzle & Streiff	33,992.58		

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Depreciation of buildings	₱ 2,167.20	
Traveling Expenses	(6,458.83)	
Transportation and representation expenses	(14,764.59)	₱ 114,672.58
Total Net Income		₱ 935,875.09
Tax due on above		₱ 254,045.00
Tax already paid		221,937.00
Deficiency		₱ 32,108.00

S u m m a r y

1949	₱ 16,008.30
1950	27,157.00
1951	38,888.00
1952	32,092.00
1953	32,108.00
Total deficiency tax due	₱146,253.30

SO ORDERED.

Manila, Philippines, July 31, 1956.

MARIANO NABLE
Presiding Judge

WE CONCUR:

AUGUSTO M. LUCIANO
Associate Judge

ROMAN M. UMALI
Associate Judge

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