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P.I. MANUFACTURING, INC.,
Petitioner,

- versus - C.T.A. CASE NO. 2500

THE COMMISSIONER OF INTERNAL REVENUE,
Respondent.

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12/27/85

D E C I S I O N

Petitioner P.I. Manufacturing, Inc., appeals from a decision dated January 15, 1973 of respondent Commissioner of Internal Revenue denying its protest against an assessment for deficiency income tax and 25% surtax for improper accumulation of profits or surplus, both for the fiscal year ended June 30, 1965, in the respective amounts of ₱114,377.40 and ₱883,191.06.

On May 12, 1975, however, the deficiency income tax of ₱114,377.40, on a motion for summary judgment by petitioner, was declared by this Court of no force and effect after finding it barred by prescription. For determination therefore, after hearing and presentation of evidence as well as submission of memoranda by the parties, is the correctness of the assessment of ₱883,191.06 as 25% surtax for unreasonable accumulation of surplus or profits imposed under Section 25 of the National Internal Revenue Code.

Section 25(a) of the National Internal Revenue Code imposes an additional tax upon a corporation formed or availed of for the purpose of preventing the imposition of the tax upon its shareholders or the shareholders of any other corporation through the medium of permitting its gains and profits to accumulate instead of being divided or distributed. And Section 25(c) provides that the fact that earnings or profits of a corporation are permitted to accumulate beyond the reasonable needs of the business shall be determinative of the purpose to avoid the tax on shareholders unless the corporation shall prove to the contrary by a clear preponderance of the evidence.

Petitioner is a corporation duly organized and existing under Philippine law, with principal office and place of business at No. 97, Industrial Avenue, Northern Hills, Malabon, Metro Manila. It is engaged in the manufacture and sale of electrical appliances and plumbing supplies.

On October 14, 1965, petitioner whose accounting period is the fiscal year, filed its income tax return for the fiscal year ended June 30, 1965. After verification of the return and investigation of petitioner's books of accounts and other accounting records, respondent Commissioner of Internal Revenue, upon recommendation of the investigating revenue examiner, assessed and demanded from petitioner the amount of ₱883,191.06 representing surtax of 25% and ½% interest on the latter's unreasonable accumulated surplus in the amount of ₱2,993,867.25, computed as follows:

FY 1964-1965

Unreasonably accumulated surplus . .	₱2,993,867.25
25% surtax due thereon	₱ 748,467.00
Add: ½% monthly interest from 10-16-65 to 10-16-68	134,724.06
Total amount due and collectible . .	₱ 883,191.06

The assessment and demand were contained in a letter of respondent dated October 12, 1970.

In a letter dated December 11, 1970, petitioner protested the assessment. However, on January 15, 1973, respondent denied petitioner's protest and reiterated the demand for payment of the assessment. Hence, the petition for review.

The sole issue for decision is whether petitioner P.I. Manufacturing, Inc. was availed of in the fiscal year ended June 30, 1965 for the purpose of avoiding the imposition of the income tax on its shareholders by permitting its earnings and profits to accumulate instead of dividing and distributing them.

The pertinent provisions of Section 25 of the National Internal Revenue Code, the law under which respondent Commissioner of Internal Revenue assessed the corresponding 25% surtax for unreasonable accumulation of surplus for the fiscal year 1964-1965, read at the time as follows:

> SEC. 25. Additional tax on corporation improperly accumulating profits or surplus.- (a) Imposition of tax.- If any corporation, except banks, insurance companies, or personal holding companies, whether domestic or foreign, is formed or availed of for the purpose of preventing the imposition of the tax upon its shareholders or members or the shareholders or members of another corporation, through the medium of permitting its gains and profits to accumulate instead of being divided or distributed, there is levied and assessed against such corporation, for each taxable year, a tax equal to twenty-five per centum of the undistributed portion of its accumulated profits or surplus which shall be in addition to the tax imposed by section twenty-four, and shall be computed, collected and paid in the same manner and subject to the same provisions of law, including penalties, as that tax.
>
> xxx xxx xxx
>
> (c) Evidence determinative of purpose.- The fact that the earnings or profits of a corporation are permitted to accumulate beyond the reasonable needs of the business shall be determinative of the purpose to avoid the tax upon its shareholders or members unless the corporation, by clear preponderance of evidence, shall prove the contrary.

Since the provisions of Section 25 of the National Internal Revenue Code were bodily lifted from Section 102 of the U.S. Internal Revenue Code of 1939, including the regulations issued in connection therewith, it would be proper to refer to applicable cases decided by the

"American Federal Courts for guidance and enlightenment. (Manila Wine Merchants, Inc. vs. Commissioner of Internal Revenue, No. L-26145, Feb. 20, 1984, 127 SCRA 483.)

A prerequisite to the imposition of the tax has been that the corporation be formed or availed of for the purpose of avoiding the income tax (or surtax) on its shareholders, or on the shareholders of any other corporation by permitting the earnings and profits of the corporation to accumulate instead of dividing them among or distributing them to the shareholders. If the failure to pay dividends is due to some other cause, such as the use of the undistributed earnings and profits for the reasonable needs of the business, such purpose does not fall within the interdiction of the statute. (Mertens, Law of Federal Income Taxation, Vol. 7, Chapter 39, p. 44; See also Sec. 21, Rev. Regs. No. 2; Manila Wine Merchants, Inc. vs. Commissioner of Internal Revenue, supra.)

Inasmuch as purpose involves a state of mind or intent, it is always necessary to look at the surrounding circumstances and the attendant facts in each individual case to determine whether the purpose of the failure to make distribution was to permit the shareholders to avoid the income tax or for some other purpose, such as the use of the earnings and profits for the reasonable needs of the business. In this regard, although the testimony of the taxpayer, officers and stockholders is entitled to some weight, generally the issue is to be resolved in the light of the surrounding circumstances, including the interests of those in control and their actual conduct. (Mertens, Law of Federal Income Taxation, Vol. 7, Chapter 39, p. 45.) The applicable principles of law are clear and in the end the decision in this case must rest upon its own peculiar facts and circumstances.

The circumstances relied upon by respondent as indicating that petitioner has permitted its earnings to accumulate beyond the reasonable needs of the business are as follows: (Examiner's memorandum, Exh. "3", pp. 56-58, BIR records; See also Exh. "1", pp. 28-29 & Exh. "B", pp. 89-90, BIR records.)

a. The payment of management fees to its sister company;

b. The fact that the company has not declared dividends in the past;

c. The retention of treasury stock;

d. The fact that at the time of examination the company's financial condition warrants the declaration of dividends.

The findings of respondent's examiner with regard "to the management fees paid by petitioner to the Go Soc & Sons and Sy Gui Huat, Inc., as stated in his memorandum reports, are as follows:

> "Verification shows that the P.I. Manufacturing, Inc., is a sister corporation of the Go Soc & Sons & Sui Gue Huat, Manila and Philippine Paints, Inc., also of Malabon, Rizal. These three corporations are family corporations, in the sense that the stockholders of these three corporations are the same. The President of P.I. Manufacturing. Mrs. Cornelia Co is also one time president of Go Soc & Sons & Sui Gue Huat. The same is true with respect to Mr. Jose P. Sy. Members of the board of directors of Go Soc are likewise members of the board of directors of P.I. Furthermore, the stockholders of the three corporation are related if not by consanguinity by affinity." (Exh. "A", also Exh. "1", p. 29, BIR records.)
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> xxx xxx xxx
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> "This facts (sic) created an awkward situation which convinced the undersigned to assert that the taxpayer herein has placed itself in an untenable position. This becomes a case wherein the decisions and actuations of the officers and/or board of directors of the P.I. Manufacturing, Inc. is subject to management and review by another company whose officers and/or board of directors are the same officers being managed." (Exh. "C", p. 57, BIR records.)
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> "x x x it may be claimed in this regard that the payment of the management fee by the company to a sister company constitutes a way of or a device to deplete its surplus income for the purpose of evading the imposition of the surtax under Section 25(c) of the National Internal Revenue Code as amended." (Exh. "B", p. 89, BIR records.)

There is merit in respondent's contention. Although the deductibility of the management fees as an operating expense is no longer in issue in this case, nevertheless, it bears close scrutiny, since the payment of management fees by petitioner to a company whose controlling stockholders are one and the same as petitioner's is material to the issue on hand.

As correctly noted by respondent's examiner, the records show that the management contract between petitioner P.I. Manufacturing, Inc. and the Co Soo & Sons and Sy Gui Huat, Inc. was signed on December 20, 1963 by Sy Ching as executive vice president of the P.I. Manufacturing, Inc. and by Cornelia L. Co as president of the Co Soo & Sons and Sy Gui Huat, Inc. (p. 17, BIR records.) The income tax returns of the P.I. Manufacturing, Inc. for the fiscal year ended June 30, 1965 was signed by Cornelia L. Co as its president also. (p. 21, BIR records.)

When said examiner testified during the hearing of the case, he reiterated the same findings contained in his memorandum reports and insisted on the connection of the payment of management fees to the issue of unreasonable accumulation of surplus. Upon cross examination, counsel for petitioner failed to discredit "the testimony of the above witness for respondent, neither did the former present any rebuttal evidence to controvert the latter's assertions. (t.s.n., pp. 8-18, pp. 40-45, August 6, 1982.)

It appears, therefore, from the uncontradicted findings of respondent's examiner that petitioner and the Go Soc & Sons and Sy Gui Huat, Inc. have the same stockholders, the same board of directors and are closely held corporations. Corporations most vulnerable to the accumulated earnings tax have been corporations the stock of which was owned or controlled by a single family or at the most by a few individuals. (Mertens, Law of Federal Income Taxation, Vol. 7, Chapter 39, p. 111.) Thus, the management fees paid by petitioner to its sister company have to be carefully examined.

By the terms of the management contract, the compensation or management fee to be paid by petitioner to the manager "for the services to be rendered by the latter to the former shall be the equivalent in pesos, Philippine Currency, of three per cent (3%) of the first one million pesos (₱1,000,000.00) of net sales for each fiscal year; and five per cent (5%) of such sales in excess of one million pesos (₱1,000,000.00)." (Management Contract, p. 18, BIR records.)

The following is an analysis of petitioner's management fees paid, total administrative and general expenses which include management fees, percentage of management fees to general and administrative expenses and net income before income taxes for the fiscal years ending June 30, 1958 through June 30, 1965, as reflected in the financial statements submitted by petitioner:

Exh. No.	Fiscal Year Ended	Management Fees	Administrative & General Expenses including Management Fees	Percentage of Management fee to Adm. and General Expenses	Net Income before Income Tax
E-2	June 30, 1958	₱147,884.32	₱281,401.35	52.55%	₱818,757.56
E-2	June 30, 1959	180,129.43	380,632.31	47.32%	1,138,495.01
F-2	June 30, 1960	199,262.72	482,306.38	41.31%	1,447,117.32
F-2	June 30, 1961	183,035.48	568,150.49	32.21%	615,488.87
G-2; G-4	June 30, 1962	262,899.00	1,058,442.32	24.83%	1,097,544.33
G-2; G-4	June 30, 1963	264,884.70	1,167,045.11	22.69%	638,228.86
H-2; H-4	June 30, 1964	267,967.30	652,725.65	41.05%	588,416.98
H-2; H-4	June 30, 1965	311,804.08	648,709.51	48.06%	1,087,985.74

The above analysis shows that the management fees paid for the fiscal year ending June 30, 1965 in the amount of ₱311,804.08 was 48.06% of the total administrative and general expenses amounting to ₱648,709.51 for that year. Had this management fee not been expended, it would have formed part of net income which would later on be credited to retained earnings. The same holds true for the management fees paid in the previous years. If these fees had not been paid they would have been substantial additions to retained earnings, since the financial statements reveal that the management fee was the largest expense incurred every year among the administrative and general expenses, except for the fiscal years ending June 30, 1962 and 1963 when it was second only to taxes and licenses. (See Exhs. "E-2", "F-2", "G-4", "H-4" and "I-4", petitioner's envelope.)

Considering that petitioner did not prove the reasonableness of its payment of such management fees to a company whose controlling stockholders are the same as petitioner's, we find respondent's stand on this matter well taken. Apparently, the close relationship between petitioner and the Go Soc & Sons and Sy Gui Huat, Inc., because of complete ownership and control by the same stockholders and the same board of directors, was used in effect for the purpose of avoiding the surtax.

With regard to the dividend distribution, petitioner claims that contrary to respondent's allegation, it had been paying substantial dividends prior to 1964 and 1965 in amounts it could afford subject to its working capital needs and its expansion program.

To trace the history of dividend distributions made by petitioner as disclosed by its financial statements, summarized in Annex "A" are petitioner's net income after taxes, adjustments to earned surplus, dividends declared and earned surplus balances for the fiscal years ending June 30, 1956 to June 30, 1965.

Note that for the years 1958, 1960, 1964 and 1965 there were no dividends declared although petitioner realized substantial profits and had sufficient earned surplus balances in those years. For the taxable years 1956, 1957, 1959, 1961, 1962 and 1963 the years when dividends were declared, all dividend distributions made were in stock, except for 1959 and 1961, when 42.48% and 50% respectively of the total dividends distributed were in cash and the balances in stock. While it is true that petitioner declared dividends in the years mentioned, its stockholders were subject to tax only on the cash dividends they received for the years 1959 and 1961.

Stock dividends even though tax exempt nevertheless capitalize earnings and result in a reduction of profits available for distribution where the purpose at the time of issuance of the stock dividend is tax avoidance. In the light of respondent's other findings, such a dividend policy as petitioner's invites judicial suspicion that the proscribed purpose most likely exists.

The principal reason advanced by petitioner for its failure to pay dividends for the years ending 1964 and 1965 was the fact that the company was constrained to acquire treasury stock of 11,116.46 shares in 1964, which was increased by a minor amount in 1965 to 11,121.6 shares, at a total cost of ₱2,043,417.22; and as a result of this acquisition of treasury stock, petitioner's dividends in 1965 were restricted to the equivalent of their acquisition cost for as long as the shares were held in treasury, pursuant to the requirement by the Securities and Exchange Commission as laid down in its rulings. (Petitioner's Memorandum, p. 204, CTA records; pp. 218-220, CTA records.)

On the other hand, respondent points out that this acquisition and retention of treasury stock is another circumstance that indicates that petitioner unreasonably accumulated its surplus.

We agree with respondent's view.

Treasury stock is customarily defined as stock of a corporation that has been legally issued as fully paid and thereafter has been reacquired by the corporation through purchase, donation or settlement of an obligation and has not been formally cancelled.

In the instant case, petitioner reacquired its stock by purchase in 1964 and held this in treasury in 1965 through 1966. As indicated in its balance sheet for 1965 (Exh. "H-1"), the redemption cost of

11,116.6 shares in 1964 was ₱2,042,522.22 which was increased to ₱2,043,447.22 in 1965 with the addition of 5 shares, bringing the total number of shares to 11,121.6. The earned surplus balances at the end of the fiscal years 1964 and 1965 were ₱2,224,277.51 and ₱2,993,867.25, respectively. (See Annex "A".) The balance sheet for the year ending June 30, 1967, with comparative figures for 1966 (Exh. "I-1"), shows under "Stockholders Equity" that these treasury shares remained in the treasury through 1966 and were sold in 1967. On the asset side of the same balance sheet are reflected two receivable accounts from stockholders in 1967 as follows:

Due from stockholders - current portion (Note 2)	₱ 458,437.37
Due from a stockholder - net of portion shown under current assets (Note 2)	₱1,407,840.00
T o t a l	₱1,866,277.37

The explanation for these accounts reads: (Exh. "I-5")

> "Note 2. Due from Stockholders
> This represents the unpaid balances on the company's treasury stock sold to stockholders together with the interest accrued thereon. A stockholder who purchased 10,871.32 shares of the treasury stock at an original amount of ₱2,011,194.20 will pay the company in sixty equal monthly installments of ₱33,520.00 until December 2, 1971 at an interest rate of 8% per annum."

Thus as of June 30, 1967, the total outstanding amount due from stockholders on account of their purchase of the treasury shares was ₱1,866,277.31 of which ₱1,407,840.00 was due from one stockholder payable in equal monthly installments up to December 2, 1971 as explained above.

The mere fact of redemption of stock furnishes no basis for imposition of the surtax. When, however, the redemption is done out of cash accumulations which reasonably may be thought excessive, such a purchase, along with other factors may appropriately be considered in arriving at the ultimate finding. (Mertens, Law of Federal Income Taxation, Vol. 7, Chapter 39, p. 75.) The touchstone of liability is the purpose behind the accumulation of the income and not the consequence of the accumulation. Thus, if the failure to pay dividends is due to some other cause such as the use of undistributed earnings and profits for the reasonable needs of the business, such purpose does not fall within the interdiction of the statute. (Manila Wine Merchants, Inc. vs. Commissioner of Internal Revenue, supra, citing Mertens, Law of Federal Income Taxation, Vol. 7, Chapter 39, pp. 45 and 47.)

The question is: Was the purpose motivating petitioner's acquisition of treasury stock in 1964 and its retention in 1965 for the reasonable needs of the business?

" To show that there was a legitimate and proper corporate object in the above acquisition of treasry stock by petitioner, witness for petitioner, its chief accountant, testified in court as follows: (t.s.n., pp. 2-4, February 12, 1980.)

"Atty. Quiogue

With the permission of this Honorable Court.

Q. Mr. Supe, during the hearing of March 5, 1979, among the reasons raised by you for justifying your company's retained earning is the acquisition by your company of treasury shares making it incapable of declaring cash dividend, as required by SEC ruling, to the extent of the cost of treasury stock. However, the acquisition of such treasury shares must be justified for some cogent reason.

Could you please enlighten us on the reasons by which your company acquired treasury shares?

A. The company was compelled to buy shares for the main reason that certain stockholders set up their own business similar to our business so that we do not want them as stockholders since they are already stockholders of competing company. And other stockholders sold their share to the company because they resign from the company.

Q. These stockholders who put up their own company, would you say that they would constitute a threat to the company if they remain as stockholders?

A. Yes. Actually they own 40 to 50% of

the ownership of the company. That would afford them substantial share in the secret of the company.

Q. Is that actually one of the reasons why your company purchased their shares?

A. Actually, they put up their own business similar to our business.

Q. Is that business still in existence?

A. That is still in existence.

JUDGE FILLER

Q. What is the name of the business?

A. Filipinas Electronics."

No competent evidence, oral or documentary, was presented by petitioner in support thereof. The bare statement of a chief accountant that some stockholders set up a business similar to petitioner's, and petitioner had to buy their shares, unaccompanied by adequate evidence, has no weight with the Court. It should be noted that an accountant is not in charge of the administration and management of a company and does not usually lay down business policies. There is no other evidence in the records which sufficiently shows that the acquisition of the treasury stock was indeed for valid business reasons as alleged by petitioner. In fact, the said purchase of treasury shares was a drain on petitioner's financial resources, in view of the substantial amount involved. And even more, said shares were retained for two years, 1965 to 1966, in the treasury, after which they were sold on account to petitioner's stockholders in 1967, particularly to one stockholder at an original amount of ₱2,011,191.20, payable in sixty equal monthly installments until December 2, 1971 at an interest rate of 8% per annum.

While evidence of what the taxpayer in fact did subsequent to the taxable year does not of itself prove or disprove the reasonableness of an accumulation in the taxable year, it bears upon the weight to be attached to the evidence of the taxpayer's intentions in the taxable year. (Mertens, Law of Federal Income Taxation, Vol. 7, Chapter 39, p. 78.)

It is thus clear beyond doubt that petitioner financed the sale of its treasury stock to its stockholders. Corporate funds were utilized in the transaction to enable its stockholders to purchase the treasury stock on credit. All the other circumstances which might be construed as evidence of the purpose to avoid the tax on shareholders cannot be outlined, but among other things, dealings between the corporation and its shareholders, such as withdrawals by the shareholders as personal loans or the expenditure of funds by the corporation for the personal benefit of the stockholders are considered. (Sec. 19, Rev. Regs. No. 2.)

There was no proof that the acquisition of treasury stock was for the real and immediate benefit of petitioner. On the contrary, it appears that the said acquisition was for the benefit of the stockholders.

A highly important factor of proof in connection with a purpose to escape tax on the stockholder is the presence of loans made to stockholders; such loans tend to prove the lack of necessity of the accumulation of surplus by the corporation. It has been held to be immaterial that the stockholder is willing to pay a higher rate of interest than banks or other third parties, or that the stockholder guarantees to pay interest. Quite naturally the question immediately arises as to why the corporation does not pay dividends to its stockholders if it is able to make loans to them out of its earnings and profits. (Mertens, Law of Federal Income Taxation, Vol. 7, Chapter 39, p. 71.)

It is clear from the foregoing that in retaining its treasury shares in 1965 for the purpose of selling them on credit to its stockholders, petitioner has allowed its earnings and profits to accumulate beyond the reasonable needs of the business, which is determinative of the purpose to avoid the tax on its shareholders.

"   The other grounds cited by petitioner to justify its accumulation of earnings were its long range expansion program and its need for more working capital. It is argued by petitioner that its surplus has in fact been plowed back into its business in the form of fixed assets acquired in pursuance of a long-range expansion program.

To evidence the implementation of its long range program, petitioner introduced extensive exhibits showing the various additions to its fixed assets from July 1, 1958 to June 30, 1967 amounting to ₱3,790,720.77. However, petitioner did not submit proofs of specific, definite and feasible plans for the accumulation in the taxable year in question. Thus:

> "To determine the 'reasonable needs' of the business in order to justify an accumulation of earnings, the Courts of the United States have invented the so-called 'Immediacy Test' which construed the words 'reasonable needs of the business' to mean the immediate needs of the business, and it was generally held that if the corporation did not prove an immediate need for the accumulation of the earnings and profits, the accumulation was not for the reasonable needs of the business, and the penalty tax would apply." (Manila Wine Merchants, Inc. v. Commissioner of Internal Revenue, supra.)

Such plans as the corporation has for use of accumulated earnings must be in existence at the close of the year in which the accumulation is made. In order to determine whether profits were accumulated for the reasonable needs of the business or to avoid the surtax upon shareholders, the controlling intention of the taxpayer is that which is manifested at the time of the accumulation, not subsequently declared intentions which are merely the products of afterthought. (Basilan Estates, Inc. vs. Commissioner of Internal Revenue, 21 SCRA 17 citing Jacob Mertens, Jr., The Law of Federal Income Taxation, Vol. 7, Cumulative Supplement, p. 213.)

Petitioner placed great emphasis on the use of the "Bardahl" formula to ascertain its working capital needs for one business cycle. Applying the Bardahl formula, petitioner tried to show that it needed funds to provide working capital in the amount of ₱4,672,118.06 for one operating cycle. (Exh. "J".) Since its net liquid assets as of the end of the tax year 1965 was only ₱3,152,165.30 (Exh. "H-1"), the shortage of working capital amounted to ₱1,519,952.76. (Petitioner's Memorandum, p. 216, CTA records.)

The use of a substantial part of petitioner's funds to acquire treasury stock and the restriction of its earned surplus as a consequence of the retention of said stock in 1965 is inconsistent with petitioner's claimed shortage of working capital. If petitioner was in dire need of funds, then it should not have burdened itself with the purchase of treasury stock and then facilitated its sale on credit to its stockholders. The sale of said shares could have been made directly from the withdrawing stockholders to the remaining stockholders, without coursing the transaction through the corporation and the end result would have been the same.

Under Section 25(c), although the existence of an accumulation beyond the reasonable business needs is determinative of the purpose to avoid the tax upon shareholders, the taxpayer may overcome the presumption by proving to the contrary by a clear preponderance of the evidence. The taxpayer's evidence must be directed to a complete lack of the proscribed purpose, as the existence of even a bonafide business purpose is not inconsistent with another purpose to reduce the surtax burden of its shareholders. (Mertens, Law of Federal Income Taxation, Vol. 7, Chapter 39, p. 53.)

What was held in Pelton Casting Co., 28 TC 153 (1957), aff'd 251 F2d 278 (CA 7th, 1958), citing Trico Products Corporation, 46 B.T.A. 346, 374 (1942), is appropriate here and we quote:

> "If the reasonable needs of the business are to be relied upon as a means of convincing us of the complete innocence

> of petitioner's purpose, this must at least require a demonstration that there was a purpose to provide for those business needs so satisfying and persuasive that it is unnecessary to look further for a motive for the action under criticism. And to this it must be added that a demonstrated purpose may be 'not inconsistent with another purpose to reduce income taxes by having a corporation accumulate its gains and profits rather than distribute them.' * * * And 'it is to this complete lack of the condemned purpose that its evidence must be directed and if it does not fairly prove an absence of such purpose it must fail regardless of what other purposes it may prove.' * * *
>
> Even if they satisfied us that the accumulations were caused in part by the plan or purpose to provide for reasonable business needs, there would remain to be examined what is expressly advanced as the principal purpose. The incidental ones would still appear as excuses, or afterthoughts, rather than evidence of an absence of the purpose described by the statute."

The Court recognizes that in consonance with well-established principles, the Commissioner's determination is presumptively correct and casts upon petitioner the burden of offering evidence in opposition thereto. The burden of proof is on the taxpayer contesting the validity or correctness of an assessment to prove not only that the Commissioner of Internal Revenue is wrong but that he (taxpayer) is right. (Lino Gutierrez vs. Collector of Internal Revenue, CTA Case No. 504, January 28, 1962; Tan Guan vs. Court of Tax Appeals, L-23676, April 27, 1967, 19 SCRA 903; Wilfredo L. Caresosa vs. Bureau of Internal Revenue, etc., CTA Case No. 3713, January 25, 1985, certiorari denied in G.R. No. 70758, Aug. 21, 1985.) And under Section 25(e) of the Revenue Code, *supra*, the fact that the earnings or profits of a corporation are permitted to accumulate beyond the reasonable needs of the business shall be determinative of the purpose to avoid the tax upon its shareholders or members unless the corporation, by clear preponderance of evidence, shall prove the contrary. Once such evidence is presented, the question thus is whether under all the evidence, petitioner has sustained by clear preponderance of evidence the burden which the statute places upon it to overcome the presumption that it was availed of for the prohibited purpose. Such presumption arises by virtue of a finding that petitioner accumulated profits beyond the reasonable needs of its business.

When we consider the peculiar facts and circumstances of the case as discussed above - payment of management fees to its sister company; history of dividend distributions made by petitioner from June 30, 1956 to June 30, 1965; retention of treasury stock and subsequent sale on credit thereof to stockholders;

absence of specific, definite and feasible plans for the accumulation in the taxable year in question - all of these facts and circumstances, taken together, tend to support the conclusion that petitioner was availed of in the fiscal year ending June 30, 1965 for the purpose of preventing the imposition of the tax upon its shareholders. And because of petitioner's failure to sustain the burden which the law applicable places upon it to overcome by clear preponderance of evidence, the determination of respondent that petitioner was availed of for the prohibited purpose in the fiscal year in question, must be sustained.

Accordingly, petitioner P.I. Manufacturing, Inc., is hereby ordered to pay to respondent Commissioner of Internal Revenue the amount of P383,191.06 representing surtax for petitioner's improper accumulation of surplus for the fiscal year 1964-1965, plus surcharges and interest incident to delinquency pursuant to the provisions of Section 51(e) of the applicable National Internal Revenue Code, as amended.

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

SO ORDERED.

Quezon City, Metro Manila, December 27, 1985.

AMANTE FILLER
Presiding Judge

WE CONCUR:

CONSTANTE C. ROAQUIN
Associate Judge

ALEX Z. REYES
Associate Judge

ANNEX "A"

Exhibit No.	Fiscal Year Ended	Net Income after Taxes	Other Adjustments to Earned Surplus	Current Earnings Available for Dividends	Dividends Paid Cash	Dividends Paid Stock	Earned Surplus Balances at the end of the year (after dividends)
C	June 30, 1956	₱ 485,987.67	-	₱ 485,987.67	-	₱ 50,000.00	₱ 597,729.80
D	June 30, 1957	649,236.68	-	649,236.68	-	850,000.00	396,966.48
E-1	June 30, 1958	724,611.56	₱ 400.00	724,211.56	-	-	1,121,978.04
E-1	June 30, 1959	891,567.01	-	891,567.01	₱554,880.00	751,200.00	707,465.05
F-1	June 30, 1960	1,021,397.32	-	1,021,397.32	-	-	1,728,862.37
F-1	June 30, 1961	438,791.87	-	438,791.87	325,050.00	325,050.00	1,517,554.24
G-1	June 30, 1962	776,276.33	-	776,276.33	-	336,272.40	1,937,558.17
G-1	June 30, 1963	454,676.86	-	454,676.86	-	587,849.50	1,804,385.53
H-1	June 30, 1964	419,891.98	-	419,891.98	-	-	2,224,277.51
H-1	June 30, 1965	769,589.74	-	769,589.74	-	-	2,993,867.25