

Title: ****Basilan Estates, Inc. vs. Commissioner of Internal Revenue and Court of Tax Appeals****

Facts:

Basilan Estates, Inc., a Philippine corporation engaged in the coconut industry, filed its 1953 income tax returns on March 24, 1954, paying an income tax of ₱8,028. On February 26, 1959, based on an examiner's report, the Commissioner of Internal Revenue assessed a deficiency income tax of ₱3,912 for 1953 and an additional 25% surtax of ₱86,876.85 on unreasonably accumulated profits for 1953 pursuant to Section 25 of the Tax Code. Due to non-payment, a warrant of distraint and levy was issued but not executed after the Deputy Commissioner ordered a constructive embargo. Subsequent to the corporation's refusal to waive the prescription period, the request for reinvestigation was denied, and on December 2, 1960, enforcement of the warrant was announced.

On December 20, 1960, Basilan Estates, Inc. petitioned the Court of Tax Appeals (CTA) for a review, alleging prescription for assessment and collection, error in disallowing depreciations and expenses, and incorrect surcharge on accumulated profits. The CTA found no prescription and affirmed the assessments. The case was appealed to the Supreme Court on February 21, 1964.

Issues:

1. Did the Commissioner's right to collect the deficiency income tax prescribe?
2. Was the disallowance of the claimed deductions for depreciation and expenses proper?
3. Were there unreasonably accumulated profits warranting the 25% surtax solely for 1953 or for accumulations from 1947-1953?
4. Is Basilan Estates, Inc. exempt from the penalty tax under Republic Act 1823 amending Section 25 of the Tax Code?

Court's Decision:

1. ****Prescription:****

- The Supreme Court ruled there was no prescription. Despite Basilan Estates arguing on receiving the notice beyond the five-year period, the Court found evidence indicating the notice was mailed on February 26, 1959. According to Section 331 of the Tax Code, assessment is made upon sending, not receipt of the notice.

2. ****Disallowance of Depreciation:****

- The Court upheld the Commissioner's decision. Depreciation should be based on

acquisition cost, not reappraised value. Deductions over acquisition cost are unjustified as depreciation allowance aims to recover only the capital investment without allowing profit beyond initial investment.

3. **Disallowance of Expenses:**

- The disallowance of ₱9,059.57 for miscellaneous and traveling expenses was overruled. The taxpayer was justified in not keeping records beyond five years as permitted under Section 337 of the Tax Code.

4. **Unreasonably Accumulated Profits:**

- The Court held there was unreasonably accumulated profit in 1953 amounting to ₱347,507.01. The determination considered the reversion of previously reserved funds without intent for reinvestment and large withdrawals by shareholders, indicating potential tax avoidance. The surtax was properly imposed and must be computed for the period reviewed.

5. **Exemption Under Republic Act 1823:**

- The exemption under Republic Act 1823 did not apply to the 1953 assessment as it was enacted in 1957, well after the period in question.

Doctrine:

1. Notice of tax assessment under Section 331 is considered issued upon mailing, not upon receipt by the taxpayer.
2. Depreciation deductions should be based on the acquisition cost of assets and not on their reappraised values.
3. Taxpayers should maintain records supporting expense claims for the period specified by law; failure to keep such documents beyond this period should not negate valid expense claims.
4. Accumulated profits can be taxed if found unreasonable under Section 25, considering prior accumulations and current financial needs.
5. Legislative changes providing tax exemptions apply prospectively and do not affect previous tax liabilities.

Class Notes:

- **Statutory Provisions:**
- Section 25 of the Tax Code: Imposes a surtax on unreasonably accumulated profits.
- Section 30(f)(1) of the Tax Code: Governs allowable depreciation deductions limited to

acquisition cost.

- Section 331 of the Tax Code: Stipulates the five-year prescription period for assessment.
- **Key Legal Principles**:
 - **Assessment Regularity**: Presumption of the regularity of official acts.
 - **Depreciation Basis**: Recovery limited to acquisition cost, not reappraised value.
 - **Documentation Period**: Tax documentation must only be preserved as required by law.
 - **Accumulated Profits**: Consideration of total financial status and previous accumulations when assessing reasonableness.

Historical Background:

The context of this case falls within the period where the Philippine tax system was evolving in its rigor and enforcement mechanisms. Post-World War II, businesses sought to rebuild, and the Government aimed to ensure accurate tax collection amidst rising economic activity. The decision underscores a stringent interpretation to curb tax avoidance schemes and enforce compliance within the bounds of the law.