

PLARIDEL SURETY & INSURANCE COMPANY, PETITIONER, VS. COMMISSIONER OF INTERNAL REVENUE, RESPONDENT.*G.R. No. L-21520. December 11, 1967*

Ponente: BENGZON, J.P., J.

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Petitioner Plaridel Surety & Insurance Co., is a domestic corporation engaged in the bonding business. On November 9, 1950, petitioner, as surety, and Constancio San Jose, as principal, solidarily executed a performance bond in the penal sum of P30,600.00 in fa-vor of the P.L. Galang Machinery Co., Inc., to secure the performance of San Jose's contractual obligation to produce and supply logs to the latter.

To afford itself adequate protection against loss or damage on the performance bond, petitioner required San Jose and one Ramon Cuervo to execute an indemnity agreement obligating themselves, solidarily, to indem-nify petitioner for whatever liability it may incur by reason of said performance bond. Accordingly, San Jose constituted a chattel mortgage on logging machineries and other movables in petitioner's favor[1] while Ramon Cuervo executed a real estate mortgage.[2]

San Jose later failed to deliver the logs to Galang Machinery[3] and the latter sued on the performance bond. On October 1, 1952, the Court of First Instance adjudged San Jose and petitioner liable; it also direc-ted San Jose and Cuervo to reimburse petitioner for whatever amount it would pay Galang Machinery. The Court of Appeals, on June 17, 1955, affirmed the judgment of the lower court. The same judgment was likewise affirmed by this Court[4] on January 11, 1957 except for a slight modification apropos the award of attorney's fees.

On February 19 and March 20, 1957, petitioner effec-ted payment in favor of Galang Machinery in the total sum of P44,490.00 pursuant to the final decision.

In its income tax return for the year 1957, petitio-ner claimed the said amount of P44,490.00 as deductible loss from its gross income and, accordingly, paid the amount of P136.00 as its income tax for 1957.

The Commissioner of Internal Revenue disallowed the claimed deduction of P44,490.00 and assessed against pe-titioner the sum of P8,898.00, plus interest, as deficiency income tax for the year 1957. Petitioner filed its protest which was denied. Whereupon, appeal was taken to the Tax Court, petitioner insisting that the P44,490.00 which it paid to Galang Machinery was a de-ductible loss.

The Tax Court dismissed the appeal, ruling that pe-titioner was duly compensated for otherwise than by in-surance - thru the mortgages in its favor executed by San Jose and Cuervo - and it had not yet exhausted all its available remedies, especially as against Cuervo, to mi-nimize its loss. When its motion to reconsider was de-nied, petitioner elevated the present appeal.

Of the sum of P44,490.00, the amount of P30,600.00 - which is the principal sum stipulated in the performance bond - is being claimed as loss deduction under Sec. 30(d)(2) of the Tax Code and P10,000.00 - which is the interest that had accrued on the principal sum - is now being claimed as interest deduction under Sec. 30(b)(1).

Loss is deductible only in the taxable year it actually happens or is sustained. However, if it is compensable by insurance or otherwise, deduction for the loss suffered is postponed to a subsequent year, which, to be precise, is that year in which it appears that no compensation at all can be had, or that there is remaining or net loss, i.e., no full compensation.[5]

There is no question that the year in which the petitioner Insurance Co. effected payment to Galang Machinery pursuant to a final decision occurred in 1957. However, under the same court decision, San Jose and Cuervo were obligated to reimburse petitioner for whatever payments it would make to Galang Machinery. Clearly, petitioner's loss is compensable otherwise (than by insurance). It should follow, then, that the loss deduction can not be claimed in 1957.

Now, petitioner's submission is that its case is an exception. Citing *Cu Unjieng Sons, Inc. v. Board of Tax Appeals*,[6] and American cases also, petitioner argues that even if there is a right to compensation by insurance or otherwise, the deduction can be taken in the year of actual loss where the possibility of recovery is remote. The pronouncement, however, to this effect in the *Cu Unjieng* case is not as authoritative as petitioner would have it since it was there found that the tax-payer had no legal right to compensation either by insurance or otherwise.[7] And the American cases cited[8] are not in point. None of them involved a taxpayer who had, as in the present case, obtained a final judgment against third persons for reimbursement of payments made. In those cases, there was either no legally enforceable right at all or such claimed right was still to be, or being, litigated.

On the other hand, the rule is that loss deduction will be denied if there is a measurable right to compensation for the loss, with ultimate collection reasonably clear. So where there is reasonable ground for reimbursement, the taxpayer must seek his redress and may not secure a loss deduction until he establishes that no recovery may be had.[9] In other words, as the Tax Court put it, the taxpayer (petitioner) must exhaust his remedies first to recover or reduce his loss.

It is on record that petitioner had not exhausted its remedies, especially against Ramon Cuervo who was solidarily liable with San Jose for reimbursement to it. Upon being prodded by the Tax Court to go after Cuervo, Hermogenes Dimaguiba, president of petitioner corporation, said that they would[10] but no evidence was submitted that anything was really done on the matter. More-over, petitioner's evidence on remote possibility of recovery is fatally wanting. Its right to reimbursement is not only secured by the mortgages executed by San Jose and Cuervo but also by a final and executory judgment in the civil case itself. Thus, other properties of San Jose and Cuervo were subject to levy and execution. But no writ of execution, satisfied or unsatisfied, was ever submitted. Neither has it been established that Cuervo was insolvent. The only evidence on record on the point is Dimaguiba's testimony that he does not really know if Cuervo has other properties.[11] This is not substantial proof of insolvency. Thus, it was too premature for petitioner to claim a loss deduction.

But assuming that there was no reasonable expectation of recovery, still no loss deduction can be had. Sec. 30(d)(2) of the Tax Code requires a charge-off as one of the conditions for loss deduction:

"In the case of a corporation, all losses actually sustained and charged-off within the taxable year and not compensated for by insurance or otherwise." (Stress supplied)

Mertens[12] states only four (4) requisites because the United States Internal Revenue Code of 1939[13] has no charge-off requirement. Sec. 23(f) thereof provides merely:

"In the case of a corporation, losses sustained during the taxable year and not compensated for by insurance or otherwise."

Petitioner, who had the burden of proof[14] failed to adduce evidence that there was a charge-off in connection

with the P44,490.00 - or P30,600.00 - which it paid to Galang Machinery.

In connection with the claimed interest deduction of P10,000.00, the Solicitor General correctly points out that this question was never raised before the Tax Court. Petitioner, thru counsel, had admitted before said court^[15] and in the memorandum it filed^[16] that the only issue in the case was whether the entire P44,490.00 paid by it was or was not a deductible loss under Sec. 30(d)(2) of the Tax Code. Even in petitioner's return, the P44,490.00 was claimed wholly as losses on its bonds.^[17] The alleged interest deduction not having been properly litigated as an issue before the Tax Court, it is now too late to raise and assert it before this Court.

WHEREFORE, the appealed decision is, as it is here-by, affirmed. Costs against petitioner Plaridel Surety & Insurance Co.

SO ORDERED.

Concepcion, C.J., Reyes, JBL, Dizon, Makalintal, Zaldivar, Sanchez, Ruiz Castro, Angeles, and Fernando, JJ., concur.

[1] Exh. K, C.T.A. Records, pp. 71-72.

[2] Exh. L, C.T.A. Records, pp. 74-76.

[3] Short for P.L. Galang Machinery Co., Inc.

[4] Plaridel Surety & Insurance Co., Inc. v. P.L. Galang Machinery Co., Inc., 100 Phil. 679.

[5] See: Sec. 30(d)(2), Int. Rev. Code; Rev. Regulations No. 2, Secs. 94 & 96; Cu Unjieng Sons, Inc. v. Board of Tax Appeals, 100 Phil. 1.

[6] Supra, Note 5.

[7] 100 Phil. 1, at 15-19, 23.

[8] Petitioner's brief, p. 18.

[9] 5 Mertens (1956 ed.), Chap. 28, pp. 19, 21.

[10] Sessions of Sept. 18, 1962, T.S.N., pp. 49-51.

[11] Ibid., T.S.N., pp. 52-53.

[12] 5 Mertens (1956 ed.), Chap. 28, p. 9.

[13] 26 U.S.C.A, 10.

[14] 5 Mertens (1956 ed.), Chap. 28, pp. 7-8.

[15] Session of Sept. 17, 1962, T.S.N., p. 2.

[16] C.T.A. Records, p. 83.

[17] See B.I.R. Records, pp. 5, 8, 14-16, 20, 22.

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