

THE COLLECTOR OF INTERNAL REVENUE, PETITIONER, VS. CANTILAN LUMBER COMPANY, RESPONDENT.

G.R. No. L-14393. October 31, 1960

Ponente: BARRERA, J.

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BARRERA, J.:

This is an appeal taken by petitioner Collector of Internal Revenue from the decision of the Court of Tax Appeals (in C.T.A. Case No. 269), holding respondent Cantilan Lumber Company, not liable for the payment of compensating tax on certain machinery and equipment purchased from the U.S. Government by the partnership "Cantilan Lumber Company".

The records disclose that on June 17, 1946, the Cantilan Lumber Company, a duly registered partnership composed of Nelson E. Kellogg and Alonso M. Villalba, entered into a contract with the U.S. Government, through the Manila Engineer District (MANED), for the supply by the former to the latter of a minimum of 2,400,000 board feet of timber. To enable the partnership to perform the terms of said contract, the U.S. Government promised to furnish to it the necessary machinery, equipment, and supplies at prices to be agreed upon by both parties.

Pursuant to said contract, the U.S. Government, through the MANED, furnished the partnership, during the 4th quarter of 1946 and the 1st quarter of 1947, various equipment such as sawmill machinery, trucks, power control unit, tractors, arch, generator, welder arc, materials and supplies with a total value of ₱262,857.78. The Collector, in his letter dated May 31, 1947, demanded from the partnership payment of the sum of ₱13,142.89, as compensating tax on the aforesaid articles.

Subsequently, the MANED made several other deliveries, thus increasing the value of the articles delivered to ₱455,078.62. Later, BIR Agent Castor Jongko reported the return by the Lumber company to MANED of certain machinery and equipment, thereby reducing the value to ₱430,785.28. Based on this last amount, the Collector, in his letter dated September 14, 1954, assessed the amount of ₱21,539.36 (5% of ₱430,785.28), as compensating tax. This demand superseded the original demand dated May 31, 1947.

The original contract (No. W-2557-eng-409) between MANED and the partnership was modified by a supplemental agreement dated July 16, 1947, known as Modification No. 1, and by supplemental agreement dated June 25, 1948, known as Modification No. 5. Modification No. 1 described the items delivered by the MANED to the partnership, and provided that payment for all items so delivered would be made by the U.S. Government, withholding any amount which became due the contractor under the contract, until the full price for said items had been paid. It also extended the term of the contract to June 30, 1948. Modification No. 5, on the other hand, made a change in the manner of delivery of the lumber, and extended the term of the original contract to May, 1949.

In the meantime, the partnership (Cantilan Lumber Company) underwent several changes. It was dissolved as of August 12, 1948, as per agreement executed on September 30, 1948, by the partners (Kellogg and Villalba), whereby Kellogg purchased for ₱80,000.00, "all of the participation, share, right, title and interest whatsoever of

him (Villalba)" "in the business and good will of the partnership hereby dissolved, and in all and singular the equipment, engines, machinery, whether fixed or movable, tools and accessories, plant, buildings and other improvements, supplies, effects, stocks of logs and .lumber, book accounts and other credits, contracts including the above-mentioned contract with the United States Government, and other assets of the partnership." One of the conditions of the sae was the agreement of Kellogg "to assume, pay and satisfy all debts and other liabilities of the partnership hereby dissolved as shown by the books of the firm as of the date of dissolution thereof, except the income taxes accrued to the date of dissolution, which taxes shall be apportioned equally between and paid by both of the parties."

On October 29, 1948, respondent Cantilan Lumber Company was duly organized and registered as a corporation[1] "for the purpose of taking over the entire lumber business previously operated by the aforesaid partnership (Cantilan Lumber Company), together with all the equipment, buildings and other properties or assets appertaining thereto." As per deed of sale executed by the parties (dated December 7,1948) Kellogg, for and in consideration of the sum of P160,000.00,[2] sold, assigned, transferred, and conveyed to respondent corporation "all the lumber business heretofore carried on by the former partnership of Kellogg and Villalba under the name and style of 'Cantilan Lumber Company,' and all and singular the equipment, engines, machinery, whether fixed or movable tools and accessories, plant, buildings and other improvements, supplies, effects, stocks of logs and lumber, book accounts and other credits, contracts including Contract No. W-2557-eng-409 dated June 17, 1946; with the Government of the United States of America for the supplying of Philippine hardwood lumber, and other assets of said partnership of every nature and description including good-will and trade-name, the said assets being understood as those appearing on the books of account and inventories of said (partnership) business as of the 12th of August, 1948." One of the conditions of the sale was the agreement by respondent corporation "to discharge all lawful debts and liabilities of the Vendor (Kellogg) in relation to the said lumber business as shown by the books of the firm as of the date of said transfer (August 12, 1948)." Kellogg was one of the original directors of respondent corporation, owning 40% of the subscribed capital stock thereof, and its general manager.

As heretofore stated, as early as May 31, 1947, petitioner demanded payment of the compensating tax on the aforementioned machinery, equipment, and supplies. However, collection of the said tax could not be made as the Cantilan Lumber Company (the partnership as well as the corporation) through its general manager Kellogg interposed the defense that the machinery and equipment were still owned by the U. S. Government.

On September 14, 1954, after a revision of the account, petitioner, in his letter addressed to respondent corporation, again demanded payment of the tax, this time in the increased sum of P21,539.26, in view of additional machineries and equipment delivered to the corporation. Respondent, in its letter addressed to the Bureau of Internal Revenue dated October 21, 1954 and signed by its then general manager, G.W. Bayer, replied that it has not yet obtained title to the property, inasmuch as it was still indebted to the U. S. Government, and requested petitioner to hold the matter in abeyance, until they hear from Washington regarding the claim, in order that they can ascertain the final and actual amount of the compensating tax for which the corporation may be liable.

It appears, however, that title to the machinery and equipment in question was transferred to respondent corporation, when it was already a corporation, on May 11, 1954.

On November 18, 1955, the Deputy Provincial Treasurer of Surigao, acting upon petitioner's instruction, seized the following property of respondent corporation:

One (1) Unit Sawmill, complete with edger, 7-1/2 "American"

P43,000.00

One (1) Unit Caterpillar Power Plant, D-17000, 8 cyl., camp.....

16,000.00

P59,000.00

pursuant to the Warrant of Distrainment and Levy issued by petitioner on December 6, 1954, to satisfy the said sum of P21,539.26.

On November 28, 1955, respondent corporation requested petitioner, in writing, that the assessment of the compensating tax against it be withdrawn or cancelled, and that the distrainment and levy upon its property be lifted, on the grounds that (1) it is not liable for said tax; (2) the warrant of distrainment and levy is illegal and void; and (3) even assuming, arguendo, that it could be held liable therefor, its collection by distrainment and levy is barred by the statute of limitations. On March 27, 1956, petitioner rendered his decision denying said request.

On May 7, 1956, respondent corporation filed with the Court of Tax Appeals, a petition for review. In due time and after trial, the Court of Tax Appeals rendered a decision which, in part, reads:

"The rule is well-established that under this law (Sec. 190, Tax Code), articles purchased from the U.S. Government, or from any of its agencies or instrumentalities in the Philippines, are subject to the corresponding compensating tax, sales tax, or specific tax, as the case may be (Go Cheng Tee vs. Meer, 87 Phil., 18; 47 Off. Gaz. 269; Saura Import and Export Co., Inc. vs. Meer, 88 Phil., 199; P.M.P. Navigation Co. vs. Meer, 91 Phil., 32; A. Soriano y Cia vs. Collector, 97 Phil., 505; 51 Off. Gaz. [9] 4548). However, it is alleged on behalf of respondent that the compensating tax accrues and becomes payable only after the complete transfer of title to the articles from the U.S. Government to the purchaser. In this case, it is claimed that title to the articles in question was transferred only when the purchase price was fully paid by petitioner. Hence, it is petitioner which is subject to the tax.

"The position taken by respondent finds no justification in the wording of the law. The law imposes the compensating tax upon commodities, goods, ware or merchandise, except those specifically exempted, purchased or received from without the Philippines. There is nothing in the law which requires that for the tax to accrue it is essential that absolute title to the property be transferred from the person from whom it is purchased or received to the person who purchased or received it. It is enough for a person to be subject to the compensating tax that he purchased or received a taxable article from without the Philippines. Who purchased or received the articles in question from the U.S. Government? Undoubtedly, it was the Partnership and not the petitioner. The fact that the purchase price of said articles was not fully paid by the Partnership does not alter the fact that the articles were purchased and subsequently received by it. Accordingly, it is the Partnership which under the law and the facts of the case is liable for the payment of said tax.

* * * * *

"Having found that the petitioner is not subject to the compensating tax on the articles purchased and received by the Partnership, respondent was without authority to enforce collection of the tax against petitioner by distrainment of its personal property. Section 318 of the Revenue Code which empowers respondent to distrain personal property limits such power to the seizure of personal property belonging to the 'person owing any delinquent tax or delinquent revenue'. It does not extend to property belonging to a person who is not a delinquent taxpayer, as petitioner in this case. Of course, from the evidence of record, it appears that petitioner is not an innocent purchaser of the articles in question, it having acquired said articles from Nelson E. Kellogg with knowledge of the tax obligation of the Partnership, but this fact does not make petitioner personally liable

for the tax. (See *Hongkong & Shanghai Banking Corporation vs. Rafferty*, 39 Phil., 145; *Pio Barretto Sons, Inc. vs. Collector of Internal Revenue*, C.T.A. No. 75, Nov. 8, 1956.) Since the articles were acquired by petitioner subject to the lien for the compensating tax, the proper remedy is the institution of an action to enforce the lien on whatever property subject thereto before the lien is extinguished, if respondent wants to proceed against petitioner and not against the Partnership or the partners Nelson E. Kellogg and Alonso N. Villalba, or any one of them.

"Petitioner not being liable for the compensating tax assessed against it, we deem it unnecessary to pass upon the question whether or not the right of the Government to collect the tax has prescribed

"FOR the foregoing considerations, the decision appealed from is hereby reversed and the distraint of the personal property belonging to petitioner set aside. No pronouncement as to costs.

"SO ORDERED."

Not satisfied with said decision, the Collector of Internal Revenue now petitions for the review thereof.

Petitioner Collector of Internal Revenue claims that the Court of Tax Appeals erred in holding that respondent corporation is not liable for the payment of the compensating tax in question.

We find the contention meritorious. The records disclose that the dissolution of the partnership Cantilan Lumber Company was not due to the closing of its lumber business, but merely to the acquisition of Villalba's interest therein by Kellogg who, as sole owner, would "carry on" the business. Kellogg purchased all of the participation, share, right, title, and interest of Villalba in the business and goodwill of the dissolved partnership, including all the equipment, machinery, tools and accessories, plant, buildings, improvements, supplies, effects, stocks of logs and lumber, book accounts and credits, contracts, including the contracts with the United States Government, and other assets of the partnership. Under the contract of sale, Kellogg expressly agreed to assume, pay and satisfy "all debts and other liabilities of the partnership" appearing in the books of the firm at the time of its dissolution, "except the income taxes" accrued, which were to be apportioned between and paid by both parties.

Subsequently, respondent corporation was duly organized and registered as a corporation on October 29, 1948, for the express purpose of "taking over the entire lumber business previously operated by the partnership" together with all the equipment, buildings, and other properties or assets appertaining thereto. In the deed of sale (dated December 7, 1948), Kellogg (then the sole owner of all the assets and liabilities of said partnership by virtue of the sale on August 12, 1948) assigned, transferred, and conveyed to respondent corporation "all the lumber business heretofore carried, on by the former partnership of Kellogg and Villalba under the name and style of 'Cantilan Lumber Company'", including all the equipment, engines, machinery, tools and accessories, plant, buildings, improvements, supplies, effects, stocks of logs and lumber, book accounts and credits, contracts, including Contract No. W-2557-eng-409 dated June 17, 1946 with the Government of the United States of America, and other assets of said partnership of every nature and description, including goodwill and trade name. In said contract of sale, respondent corporation expressly agreed "to discharge all lawful debts and liabilities" of the vendor Kellogg, in relation to said lumber business as shown by the books of the firm on the date of the transfer or sale to Kellogg on August 12, 1948.

Thus, it is to be noted that the transfer from the partnership to Kellogg alone, and from him to the corporation, refers to the totality of the entire business of the partnership, including all the assets and liabilities of the latter and, particularly in relation with the case at bar, the contract with the United States Government relating to the purchase of the machineries and equipment subject to the tax in question. The compensating tax due from the partnership is one of these liabilities, considering that proper demand for its payment has already been made since May 31, 1947, more than a year before the changes in its organizational set-up took place. And this liability was

not ex-cepted from the transfer as was the income tax. In other words, it was assumed by the transferees. This is evident from the letter of the General Manager of respondent corporation dated October 21, 1954 (Exh. 24), or shortly after its incorporation, wherein the corporation acknowledged receipt of the Collector's demand for the payment of the compensating tax and, instead of disputing it and disclaiming liability therefor, requested that the matter be held in abeyance until it could communicate with Washington regarding the status and exact amount of its indebtedness to enable it "to determine the final and actual amount of compensating tax for which it may be liable."

It is significant to note that Kellogg, one of the partners of the dissolved partnership Cantilan Lumber Company and subsequently sole owner thereof, is one of the six original directors of the newly-organized corporation, owning 40% of its subscribed capital stock or a majority stockholder thereof. He was also its general manager at the inception and at the time of the transfer of the entire lumber business to the corporation.

All these circumstances, to our mind, conclusively indicate, not only knowledge but actual assumption by respondent corporation of the existing liability of the dissolved partnership Cantilan Lumber Company for the compensating tax in question. In this connection, the Court of Tax Appeals correctly observed that respondent corporation "is not an innocent purchaser of the articles in question, it having acquired said articles from Nelson E. Kellogg, with knowledge of the tax obligation of the Partnership."

Petitioner next contends that the Court of Tax Appeals erred in setting aside the distraint on the property involved herein.

In view of what has already been said, this contention must, likewise, be upheld. As heretofore stated, respondent corporation is liable for the payment of the compensating tax assessed. Being delinquent in the payment thereof, petitioner was, undoubtedly, justified in distraining its (respondent's) property in question on November 18, 1955, pursuant to Section 318 of the National Internal Revenue Code, to satisfy the tax. Contrary to respondent's claim, said distraint is not illegal, as it was made 1 year and 4 days from September 14, 1954, the date of the last assessment or well-within the 5-year period provided in Section 832 (c) of the same Code.

Wherefore, the decision of the Court of Tax Appeals appealed from is hereby set aside, without pronouncement as to costs. So ordered.

Paras, C.J., Bengzon, Bautista Angelo, Labrador, Reyes, J.B.L., Gutierrez David, and Paredes, JJ., concur.

Decision set aside.

[1] The Articles of Incorporation were signed on September 30, the same date the partnership was dissolved and the entire business transferred to Kellogg alone.

[2] Paid in shares of the corporation.

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