

MARCELO STEEL CORPORATION, PETITIONER, VS. COLLECTOR OF INTERNAL REVENUE, RESPONDENT.

G.R. No. 12401. October 31, 1960

Ponente: PADILLA, J.

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PADILLA, J.:

This is a petition to review under section 18, Republic Act No. 1125, a judgment of the Court of Tax Appeals upholding the assessment made by the respondent for income tax due during the yearn 1952 and 1953 from the petitioner (C.T.A. Case No. 172).

The parties have entered into a stipulation of facts, which the Court summarized as follows:

The petitioner is a corporation duly organized and existing under and by virtue of the laws of the Philippines, with offices at Malabon, Rizal. It is engaged in three (3) industrial activities, namely, (1) manufacture of wire fence, (2) manufacture of nails, and (3) manufacture of steel bars, rods and other allied steel products. During the years 1952 and 1953, the last two mentioned industrial operations, more specifically, the manufacture of nails and the manufacture of steel bars, rods and other allied steel products, enjoyed the benefits of tax exemption under Republic Act No. 35.

On May 21, 1953, the petitioner filed an income tax return for the year 1952, reflecting a net income of P34,386.58 realized solely from its business of manufacturing wire fence, an activity which is not tax exempt, and on March 31, 1954, it filed its income tax return for the year 1953, showing a net income of P58,329.00 realized from the same sources, i.e., the manufacture of wire fence.

On the basis of the said income tax returns filed by the petitioner for the years 1952 and 1953 which did not reflect the financial results of its tax exempt business activities, the respondent assessed the total sum of P12,750.00. Accordingly, the petitioner paid the said amount assessed against it on the following dates;

Tax Year

Date

Amount

1952

May 30, 1953

P3,458.50

1952

August 15, 1953

3,458.50

1953

May 15, 1954

5,833.00

Total.....12,750.00

On October 1, 1954, the petitioner filed amended income tax returns for taxable years 1952 and 1953, showing that it suffered a net loss of P871,407.37 in 1952, and P4,956.29 in 1953. The said losses were arrived at by consolidating the gross income and expenses and/or deductions of the petitioner in all its business activities, as follows:

For the year 1952

Net income, taxable industry:

Wire fence

P34,386.58

Net loss, tax exempt industries:

Nails

(P620,722.73)

Steel bars

(285,071.22)

(905,793.95)

Total Net Loss

(P871,407.37)

For the year 1953

Net income, taxable industry:

Wire fence

P58,329.11

Net loss, tax exempt industries:

Nails

(P60,950.20)

Steel bars

(102,335.20

(163,285.40)

Total Net Loss

(P104,956.29)

On October 1, 1954, the petitioner, claiming¹ that instead of earning¹ the net income shown in its original income tax returns for 1952 and 1953, it sustained the losses shown in its amended income tax returns for the same years, filed its request for refund of the income taxes for the said years amounting to P12,750.00 which it allegedly erroneously paid to the respondent.

After more than ten months of waiting without any action being taken by the respondent on the claim for refund, and in order to protect its rights under Section 306 of the National Internal Revenue Code, the petitioner, on August 13, 1955, filed with this Court the instant petition for review.

There are two issues to be resolved in this case, namely, (1) whether or not the petitioner may be allowed to deduct from the profits realized from its taxable business activities, the losses sustained by its tax exempt industries, and (2) whether or not the action for refund, with regard to the sum of P3,458.50 which was paid on May 30, 1953, has already prescribed under Section 306 of the Tax Code.

The Court of Tax Appeals held that "the petitioner cannot deduct from the profits realized from its taxable industries, the losses sustained by its tax exempt business activities,* * *."

The duration of the petitioner's tax exemption with respect to the manufacture of nails is from 25 June 1949 to 25 June 1953 (Exhibit 7), later adjusted to be from 11 August 1949 to 11 August 1953, and with respect to the manufacture of steel bars, rods and other allied steel products, is from 16 March 1951 to 16 March 1955 (Exhibit 6). The exemption refers to the following internal revenue taxes: the fixed and privilege tax on business, the percentage tax on the sales of manufactured products, in respect to which exemption was granted, the compensating tax on the articles, goods or materials exclusively used in the new and necessary industry, the documentary stamp tax and the income tax with respect to the net income derived from the exempt industry (Exhibits 6 and 7).

The petitioner's theory is that since it is a corporation organized with a single capital that answers for all its financial obligations including those incurred in the tax-exempt industries, the gross income derived from both its taxable or non-exempt and tax-exempt industries, and the allowable deductions from said incomes, should be consolidated and its income tax liability should be based on the difference between the consolidated gross incomes and the consolidated allowable deductions. It relies on the provisions of section 24, Commonwealth Act No. 466, as amended, providing that "There shall be levied, assessed, collected, and paid annually upon the total net income received in the preceding taxable year from all sources by every corporation organized in, or existing under the laws of the Philippines." a graduated tax (*Italics supplied*), and of section 30, subsection (d), paragraph (2), of the same Act providing that in computing the net income of a corporation, all losses actually sustained by it and charged off within the taxable year and not compensated for by insurance or otherwise, are allowed as deductions.

Republic Act No. 35, the law under which the petitioner was granted tax exemption for the manufacture of nails and steel bars, rods and other allied steel products, provides:

Section 1. Any person, partnership, company, or corporation who or which shall engage in a new and necessary industry shall, for a period of four years from the date of the organization of such industry, be entitled to exemption from the payment of all internal revenue taxes directly payable by such person, partnership, company, or corporation in respect to said industry.

Sec. 2. The President of the Philippines, shall, upon recommendation of the Secretary of Finance, periodically determine the qualifications that the industries should possess to be entitled to the benefits of this Act.

Sec. 3. This Act shall take effect upon its approval.

(Approved, September 30, 1946.)

The purpose or aim of Republic Act No. 35 is to encourage the establishment or exploitation of new and necessary industries to promote the economic growth of the country. It is a form of subsidy granted by the Government to courageous entrepreneurs staking their capital in an unknown venture. An entrepreneur engaging in a new and necessary industry faces uncertainty and assumes a risk bigger than one engaging in a venture already known and developed. Like a settler in an unexplored land who is just blazing a trail in a virgin forest, he needs all the encouragement and assistance from the Government. He needs capital to buy his implements, to pay his laborers and to sustain him and his family. Comparable to the farmer who has just planted the seeds of fruit bearing trees in his orchard, he does not expect an immediate return on his investment. Usually loss is incurred rather than profit made. It is for these reasons that the law grants him tax exemption to lighten onerous financial burdens and reduce losses. However these may be, Republic Act No. 35 has confined the privilege of tax exemption only to new and necessary industries. It did not intend to grant the tax exemption benefit to an entrepreneur engaged at the same time in a taxable or non-exempt industry and a new and necessary industry, by allowing him to deduct his gains or profits derived from the operation of the first from the losses incurred in the operation of the second. Unlike a new and necessary industry, a taxable or non-exempt industry is already a going concern, deriving profits from its operation, and deserving no subsidy from the Government. It is but fair that it be required to give to the (Government a share in its profits in the form of taxes.

The fact that the petitioner is a corporation organized with a single capital that answers for all its financial obligations including those incurred in the tax exempt industries is of no moment. The intent of the law is to treat taxable or non-exempt industries as separate and distinct from new and necessary industries which are tax-exempt for purposes of taxation. Section 7, Executive Order No. 341, series of 1950, issued by the President of the Philippines pursuant to section 2, Republic Act No. 35, provides:

Any industry granted tax exemption under the provisions of Republic Act No. 35 shall report to the Secretary of Finance at the end of every fiscal year a complete list and a correct Valuation of all real and personal property of its industrial plant or factory; shall file a separate income tax return; shall keep separately this accounting records relative to the industry declared -exempt; shall keep such records and submit such sworn statements as may be prescribed from time to time by the Secretary of finance;^[1] (Italics supplied.)

And when Congress revised the provisions of Republic Act No. 35 by enacting into law Republic Act No. 901 it incorporated similar provisions and provided that "Any industry granted tax exemption under the provisions of Republic Act No. 35" shall "file a separate income tax return."^[2]

The petitioner states that it is not liable to pay income tax on its industries of manufacturing nails and steel bars, rods and other allied steel products for the reason that it had incurred loss in their operation and not because it is exempt under the provision of Republic Act No. 35. It argues that by being allowed to deduct its gains derived

from the operation of its taxable or non-exempt industry of manufacturing wire fence, from the losses incurred in the operation of its tax-exempt industries of manufacturing nails and steels bars, rods and other allied steel products, it would not receive the benefit of double exemption. While the purpose of tax exemption under Republic Act No. 35 is to lighten the onerous financial burdens and reduce the losses of the entrepreneur, yet it is not designed to assure him of a return on his capital invested. As already stated, the law intended to treat taxable or non-exempt industry as separate and distinct from new and necessary industry, which is tax exempt, and did not mean to grant an entrepreneur, engaged at the same time in a taxable or non-exempt industry and a new and necessary industry, the benefit or privilege of deducting his gains or profit derived from the operation of the first from the losses incurred in the operation of the second. Moreover, aside from its exemption from the payment of income tax on its profits derived from the operation of new and necessary industries, the petitioner is exempt from the payment of other internal revenue taxes directly payable by it, such as the fixed and privilege tax on business, the percentage tax on the sales of manufactured products, in respect to which exemption is granted, the compensating tax on the articles, goods or materials exclusively used in the new and necessary industry, and the documentary stamp tax (Exhibits 6 and 7). These exemptions alone are enough to lighten its onerous financial burdens and reduce losses.

The petitioner claims that unlike the United States Internal Revenue Code which expressly forbids the deduction of-

Any amount otherwise allowable as a deduction which is allocable to one or more classes of income jpthr than interest (whether or not any amount of income of that class or classes is received or accrued) wholly exempt from the taxes imposed by this chapter. [(Section 24 (a) (5)]

our National Internal Revenue Code does not contain a similar prohibition. When in 1939 Commonwealth Act No. 466, the National Internal Revenue Code, was enacted into law, the idea of granting tax exemption to new and necessary industries in the Philippines had not yet been thought of because there were no new and necessary industries being established or exploited. It was only in 1946, after the last World War, and after the Philippines became a sovereign nation, that the establishment or exploitation of new and necessary industries was stimulated. Hence the absence of a similar provision in our National Internal Revenue Code. This absence, however, cannot be capitalized upon by the petitioner in support of its theory. For, as already stated, when Congress enacted Republic Act No. 35 into law, it intended to segregate income derived from the operation of new and necessary industries from that derived from the operation of taxable or non-exempt industries.

For the foregoing reasons, the judgment under review is affirmed, with costs against the petitioner.

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

Decision affirmed.

[1] 46 Off. Gaz. 3527, 3529.

[2] Section 7.

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