

SANTIAGO GANCAYCO, PETITIONER, VS. THE COLLECTOR OF INTERNAL REVENUE, RESPONDENT.*G.R. No. 13325. April 20, 1961*

Ponente: CONCEPCION, J.

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Petitioner Santiago Gancayco seeks the review of a decision of the Court of Tax Appeals, requiring him to pay P16,860.31, plus surcharge and interest, by way of deficiency income tax for the year 1949.

On May 10, 1950, Gancayco filed his income tax return for the year 1949. Two (2) days later, respondent Collector of Internal Revenue issued the corresponding notice advising him that his income tax liability for that year amounted P9,793.62, which he paid on May 15, 1950. A year later, or on May 14, 1951, respondent wrote the communication Exhibit C, notifying Gancayco, inter alia, that, upon investigation, there was still due from him, as deficiency income tax for the year 1949, the sum of P29,554.05. Gancayco sought a reconsideration, which was partly granted by respondent, who in a letter dated April 8, 1953 (Exhibit D), informed petitioner that his income tax deficiency for 1949 amounted to P16,860.31. Gancayco urged another reconsideration (Exhibit O), but no action was taken on this request, although he had sent several communications calling respondent's attention thereto.

On April 15, 1956, respondent issued a warrant of distraint and levy against the properties of Gancayco for the satisfaction of his deficiency income tax liability, and, accordingly, the municipal treasurer of Catanauan, Quezon, issued on May 29, 1956, a notice of sale of said properties at public auction on June 19, 1956. Upon petition of Gancayco, filed on June 16, 1956, the Court of Tax Appeals issued a resolution ordering: the cancellation of the sale and directing that the same be readvertised at a future date, in accordance with the procedure established by the National Internal Revenue Code. Subsequently, or on June 22, 1956, Gancayco filed an amended petition praying that said Court:

"(a) Issue a writ of preliminary injunction, enjoining the respondents from enforcing the collection of the alleged tax liability due from the petitioner through summary proceedings pending the determination of the present case;

"(b) After a review of the present case adjudge that the right of the government to enforce collection of any liability due on this account had already prescribed;

"(c) That even assuming that prescription had not yet set in the objections of petitioner to the disallowance of the entertainment, representation and farming expenses be allowed;

* * * * *

In his answer respondent admitted some allegations of the amended petition, denied other allegations thereof and set up some special defenses. Thereafter Gancayco received from the municipal treasurer of Catanauan, Quezon another notice of auction sale of his properties, to take place on August 29, 1956. On motion of Gancayco, the

Court of Tax Appeals, by resolution dated August 27, 1956, "cancelled" the aforementioned sale and enjoined respondent and the municipal treasurer of Catanuan, Quezon, from proceeding with the same. After appropriate proceedings, the Court of Tax Appeals rendered, on November 14, 1957, the decision adverted to above.

Gancayco maintains that the right to collect the deficiency income tax in question is barred by the statute of limitations. In this connection, it should be noted, however, that there are two (2), civil remedies for the collection of internal revenue taxes, namely: (a) by distraint of personal property and levy upon real property; and (b) by "judicial action" (Commonwealth Act 456, section 316). The first may not be availed of except within three (3) years after the "return is due or has been made * * *" (Tax Code, section 51 [d]). After the expiration of said period, income taxes may not be legally and validly collected by distraint and/or levy (Collector of Internal Revenue vs. Avelino, 100 Phil., 327; 53 Off. Gaz., 645; Collector of Internal Revenue vs. Reyes, 101 Phil., 822; Collector of Internal Revenue vs. Zulueta, 100 Phil., 872; 53 Off. Gaz., 6532. Sambrano vs. Court of Tax Appeals, 101 Phil., 1; 53 Off. Gaz., [15] 4839). Gancayco's income tax return for 1949 was filed on May 10, 1950, so that the warrant of distraint and levy issued on May 15, 1956, long after the expiration of said three-year period, was illegal and void, and so was the attempt to sell his properties in pursuance of said warrant.

The "judicial action" mentioned in the Tax Code may be resorted to within five (5) years from the date the return has been filed, if there has been no assessment, or within five (5) years from the date of the assessment made within the statutory period, or within the period agreed upon, in writing, by the Collector of Internal Revenue and the taxpayer, before the expiration of said five-year period, or within such extension of said stipulated period as may have been agreed upon, in writing, made before the expiration of the period previously stipulated, except that in the case of a false or fraudulent return with intent to evade tax or of a failure to file a return, the judicial action may be begun at anytime within ten (10) years after the discovery of the falsity, fraud or omission (Sections 331 and 332 of the Tax Code). In the case at bar, respondent made three (3) assessments: (a) the original assessment of P9,793.62, made on May 12, 1950; (b) the first deficiency income tax assessment of May 14, 1951, for P29,554.05; and (c) the amended deficiency income tax assessment of April 8, 1953, for P16,860.31.

Gancayco argues that the five-year period for the judicial action should be counted from May 12, 1950, the date of the original assessment, because the income tax for 1949, he says, could have been collected from him since then. Said assessment was, however, not for the deficiency income tax involved in this proceedings, but for P9,793.62, which he paid forthwith. Hence, there never had been any cause of judicial action against him, and, per force, no statute of limitations to speak of, in connection with said sum of P9,793.62.

Neither could said statute have begun to run from May 14, 1951, the date of the first deficiency income tax assessment for P29,554.05, because the same was, upon Gancayco's request, reconsidered or modified by the assessment made on April 8, 1953, for P16,860.31. Indeed, this last assessment is what Gancayco contested in the amended petition filed by him with the Court of Tax Appeals. The amount involved in such assessment which Gancayco refused to pay and respondent tried to collect by warrant of distraint and/or levy, is the one in issue between the parties. Hence, the five-year period aforementioned should be counted from April 8, 1953, so that the statute of limitations does not bar the present proceedings, instituted on April 12, 1956, if the same is a judicial action, as contemplated in section 316 of the Tax Code, which petitioner denies, upon the ground that

- "The Court of Tax Appeals does not have original jurisdiction to entertain an action for the collection of the tax due;
- "The proper party to commence the judicial action to collect the tax due is the government, and
- "The remedies provided by law for the collection of the tax are exclusive."

Said section 316 provides:

"The civil remedies for the collection of internal revenue taxes, fees, or charges, and any increment thereto, resulting from delinquency shall be (a) by distraint of goods, chattels, or effects, and other personal property of whatever character, including stocks and other, securities, debts, credits, bank accounts, and interest in and rights to personal property, and by levy upon real property; and (b) by judicial action. Either of these remedies or both simultaneously may be pursued in the discretion of the authorities charged with the collection of such taxes.

"No exemption shall be allowed against the internal revenue taxes in any case."

Petitioner contends that the judicial action referred to in this provision is commenced by filing, with a court of first instance, of a complaint for the collection of taxes. This was true at the time of the approval of Commonwealth Act No. 456, on June 15, 1939. However, Republic Act No. 1125 has vested the Court of Tax Appeals, not only with exclusive appellate jurisdiction to review decisions of the Collector (now Commissioner) of Internal Revenue in cases involving disputed assessments, like the one at bar, but, also, with authority to decide "all cases involving disputed assessments of Internal Revenue taxes or customs duties pending determination before the court of first instance" at the time of the approval of said Act, on June 16, 1954 (Section 22, Republic Act No. 1125). Moreover, this jurisdiction to decide all cases involving disputed assessments of internal revenue taxes and customs duties necessarily implies the power to authorize and sanction the collection of the taxes and duties involved in such assessments as may be upheld by the Court of Tax Appeals. At any rate, the same now has the authority formerly vested in courts of first instance to hear and decide cases involving disputed assessments of internal revenue taxes and customs duties. Inasmuch as those cases filed with courts of first instance constituted judicial actions, such is, likewise, the nature of the proceedings before the Court of Tax Appeals, insofar as sections 316 and 332 of the Tax Code are concerned.

The question whether the sum of P16,860.31 is due from Gancayco as deficiency income tax for 1949 hinges on the validity of his claim for deduction of two (2) items, namely: (a) for farming expenses, P27,459.00; and (b) for representation expenses, P8,933.45.

Section 30 of the Tax Code partly reads:

"(a) Expenses:

(1) In General—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; traveling expenses while away from home in the pursuit of a trade or business; and rentals or other payments required to be made as a condition to the continued use or possession, for the purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity." (Italics supplied.)

Referring to the item of P27,459, for farming expenses allegedly incurred by Gancayco, the decision appealed from has the following to say:

"No evidence has been presented as to the nature of the said 'farming expenses' other than the bare statement of petitioner that they were spent for the 'development and cultivation of (his) property'. No specification has been made as to the actual amount spent for purchase of tools, equipment or materials, or the amount spent for improvement. Respondent claims that the entire amount was spent exclusively for clearing and developing the farm which were necessary to place it in a productive state. It is not, therefore, an ordinary expense but a capital expenditure. Accordingly, it is not deductible but it may be amortized, in accordance with section 75 of Revenue Regulations No. 2, cited above. See also, section 31 of the Revenue Code which provides that in computing net income, no deduction shall in any case be allowed in respect of any amount paid out for new

buildings or for permanent improvements or betterments made to increase the value of any property or estate." (Italics supplied.)

We concur in this view, which is a necessary consequence of section 31 of the Tax Code, pursuant to which:

"(a) General Rule—In computing net income no deduction shall in any case be allowed in respect of—

"(1) Personal, living, or family expenses;

"(2) Any amount paid out for new buildings or for permanent improvements, or betterments made to increase the value of any property or estate;

"(3) Any amount expended in restoring property or in making good the exhaustion thereof for which an allowance is or has been made; or

"(4) Premiums paid on any life insurance policy covering the life of any officer or employee, or any person financially interested in any trade or business carried on by the taxpayer, individual or corporate, when the taxpayer is directly or indirectly a beneficiary under such policy." (Italics supplied.)

Said view is, likewise, in accord with the consensus of the authorities on the subject.

"Expenses incident to the acquisition of property follow the same rule as applied to payments made as direct consideration for the property. For example, commission paid in acquiring property are considered as representing part of the cost of the property acquired. The same treatment is to be accorded to amount expended for maps, abstracts, legal opinions on titles, recording fees and surveys. Other non-deductible expenses include amounts paid in connection with geological explorations, development and subdividing of real estate; clearing and grading; restoration of soil, drilling wells, architect's fees and similar types of expenditures." (4 Merten's Law of Federal Income Taxation Sec. 25.20, pp. 348-349; see also sec. 75 of the Income Regulation of the B.I.R.; (Italics supplied.)

"The cost of farm machinery, equipment and farm building represent a capital investment and is not an allowable deduction as an item of expense. Amounts expended in the development of farms, orchards, and ranches prior to the time when the productive state is reached may be regarded as investments of capital." (Merten's Law of Federal Income Taxation, supra, sec. 25.108, p. 525.)

"Expenses for clearing off and grading lots acquired is a capital expenditure, representing part of the cost of the land and was not deductible as an expense." (Liberty Baking Co. vs. Heiner, 37 F [2d] 703 [8 AFTR 10011] [CCA 3rd]; The B.L. Marble Chair Company vs. U.S., 15 AFTR 746).

"An item of expenditure, in order to be deductible under this section of the statute providing for the deduction of ordinary and necessary business expenses, must fall squarely within the language of the statutory provision. This section is intended primarily although not always necessarily, to cover expenditures of a recurring nature where the benefit derived from the payment is realized and exhausted within the taxable year. Accordingly, if the result of the expenditure is the acquisition of an asset which has an economically useful life beyond the taxable year, no deduction of such payment may be obtained under the provisions of the statute. In such cases, to the extent that a deduction is allowable, it must be obtained under the provisions of the statute which permit deductions for amortization, depreciation, depletion or loss." (W. B. Harbeson Co. 24 BTA, 542; Clark Thread Co., 28 BTA 1128 aff'd 100 F [2d] 257 CCA 3rd, 1938) 4 Martin's Law of Federal Income Taxation, Sec. 25.17, pp. 337-338."

Gancayco's claim for representation expenses aggregated P31,753.97, of which P22,820.52 was allowed, and P8,933.45 disallowed. Such disallowance is justified by the record, for, apart from the absence of receipts, invoices or vouchers of the expenditures in question, petitioner could not specify the items constituting the same, or when or on whom or on what they were incurred. The case of Cohan vs. Commissioner, 39 F (2d) 540, cited by

petitioner is not in point, because in that case there was evidence on the amounts spent and the persons entertained and the necessity of entertaining them, although there were not receipts and vouchers of the expenditures involved therein. Such is not the case of petitioner herein.

Being in accordance with the facts and law, the decision of the Court of Tax Appeals is hereby affirmed therefore, with costs against petitioner Santiago Gancayco. It is so ordered.

Padilla, Bautista Angelo, Labrador, Reyes, J.B.L., Barrera, and Dizon, JJ., concur.

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