

EL ORIENTE, FABRICA DE TABACOS, INC., PLAINTIFF AND APPELLANT, VS. JUAN POSADAS, COLLECTOR OF INTERNAL REVENUE, DEFENDANT AND APPELLEE.

G. R. No. 34774. September 21, 1931

Ponente: MALCOLM, J.

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MALCOLM, J.:

The issue in this case is whether the proceeds of insurance taken by a corporation on the life of an important official to indemnify it against loss in case of his death, are taxable as income under the Philippine Income Tax Law.

The parties submitted the case to the Court of First Instance of Manila for decision upon the following agreed statement of facts:

- That the plaintiff is a domestic corporation duly organized and existing under and by virtue of the laws of the Philippine Islands, having its principal office at No. 732 Calle Eyangelista, Manila, P. I.; and that the defendant is the duly appointed, qualified and acting Collector of Internal Revenue of the Philippine Islands.
- That on March 18, 1925, plaintiff, in order to protect itself against the loss that it might suffer by reason of the death of its manager, A. Velhagen, who had had more than thirty-five (35) years of experience in the manufacture of cigars in the Philippine Islands, and whose death would be a serious loss to the plaintiff, procured from the Manufacturers Life Insurance Co., of Toronto, Canada, thru its local agent E. E. Elser, an insurance policy on the life of the said A. Velhagen for the sum of \$50,000, United States currency.
- That the plaintiff, El Oriente, Fabrica de Tabacos, Inc., designated itself as the sole beneficiary of said policy on the life of its said manager.
- That during the time the life insurance policy here- inbefore referred to was in force and effect plaintiff paid from its funds all the insurance premiums due thereon.
- That the plaintiff charged as expenses of its business all the said premiums and deducted the same from its gross incomes as reported in its annual income tax returns, which deductions were allowed by the defendant upon a showing made by the plaintiff that such premiums were legitimate expenses of its (plaintiff's) business.
- That the said A. Velhagen, the insured, had no interest or participation in the proceeds of said life insurance policy.
- That upon the death of said A. Velhagen in the year 1929, the plaintiff received all the proceeds of the said life insurance policy, together with the interests and the dividends accruing thereon, aggregating P104,957.88.
- That over the protest of the plaintiff, which claimed exemption under section 4 of the Income Tax Law, the defendant Collector of Internal Revenue assessed and levied the sum of P3,148.74 as income tax on the proceeds of the insurance policy mentioned in the preceding paragraph, which tax the plaintiff paid under instant protest on July 2, 1930; and that defendant overruled said protest on July 9, 1930."

Thereupon, a decision was handed down which absolved the defendant from the complaint, with costs against the plaintiff. From this judgment, the plaintiff appealed, and its counsel now allege that:

- The trial court erred in holding that section 4 of the Income Tax Law (Act No. 2833) is not applicable to the present case.
- The trial court erred in reading into the law certain exceptions and distinctions not warranted by its clear and unequivocal provisions.
- The trial court erred in assuming that the proceeds of the life insurance policy in question represented a net profit to the plaintiff when, as a matter of fact, it merely represented an indemnity for the loss suffered by it thru the death of its manager, the insured."
- The trial court erred in refusing to hold that the proceeds of the life insurance policy in question is not taxable income, and in absolving the defendant from the complaint."

The Income Tax Law for the Philippines is Act No. 2833, as amended. It is divided into four chapters: Chapter I On Individuals, Chapter II On Corporations, Chapter III General Administrative Provisions, and Chapter IV General Provisions. In Chapter I On Individuals, is to be found section 4 which provides that, "The following incomes shall be exempt from the provisions of this law: (a) The proceeds of life insurance policies paid to beneficiaries upon the death of the insured * * * ." Section 10, as amended, in Chapter II On Corporations, provides that, "There shall be levied, assessed, collected, and paid annually upon the total net income received in the preceding calendar year from all sources by every corporation * * * a tax of three per centum upon such income * * * ." Section 11 in the same chapter, provides the exemptions under the law, but neither here nor in any other section is reference made to the provisions of section 4 in Chapter I.

Under the view we take of the case, it is sufficient for our purposes to direct attention to the anomalous and vague condition of the law. It is certain that the proceeds of life insurance policies paid to individual beneficiaries upon the death of the insured are exempt. It is not so certain that the proceeds of life insurance policies paid to corporate beneficiaries upon the death of the insured are likewise exempt. But at least, it may be said that the law is indefinite in phraseology and does not permit us unequivocally to hold that the proceeds of life insurance policies received by corporations constitute income which is taxable.

The situation will be better elucidated by a brief reference to laws on the same subject in the United States. The Income Tax Law of 1916 extended to the Philippine Islands. It was natural, therefore, for the Philippine Legislature, when it came to enact Act No. 2833, to copy the American statute. Subsequently, the (congress of the United States enacted its Income Tax Law of 1919, in which certain doubtful subjects were clarified. Thus, as to the point before us, it was made[^]clear, when not only in the part of the law concerning individuals were exemptions provided for beneficiaries, but also in the part concerning corporations, specific reference was made to the exemptions in favor of individual thereby making the same applicable to corporations. This was authoritatively pointed out and decided by the United States Supreme Court in the case of United States vs. Supplee-Biddle Hardware Co. ([1924], 265 U. S., 189), which involved facts quite similar to those before us. We do not think the decision of the higher court in this case is necessarily controlling on account of the divergences noted in the federal statute and the local statute, but we do find in the decision certain language of a general nature which appears to furnish the clue to the correct disposition of the instant apical. Conceding, therefore, without necessarily having to decide, that assignments of error Nos. 1 and 2 are not well taken, we would turn to the third assignment of error.

It will be recalled that El Oriente, Fabrica de Tabacos, Inc., took out the insurance on the life of its manager, who had had more than thirty-five years' experience in the manufacture of cigars in the Philippines, to protect itself

against the loss it might suffer by reason of the death of its manager. We do not believe that this fact signifies that when the plaintiff received P104,957.88 from the insurance on the life of its manager, it thereby realized a net profit in this amount. It is true that the Income Tax Law, in exempting individual beneficiaries, speaks of the proceeds of life insurance policies as income but this is a very slight indication of legislative intention. In reality, what the plaintiff received was in the nature of an indemnity for the loss which it actually suffered because of the death of its manager.

To quote the exact words in the cited case of Chief Justice Taft delivering the opinion of the court:

"It is earnestly pressed upon us that proceeds of life insurance paid on the death of the insured are in fact capital, and cannot be taxed as income under the Sixteenth Amendment. *Eisner vs. Macomber*, 252 U. S., 189, 207; *Merchants' Loan & Trust Co. vs. Smietanka*, 255 U. S., 509, 518. We are not required to meet this question. It is enough to sustain our construction of the act to say that proceeds of a life insurance policy paid on the death of the insured are not usually classed as income.

"* * * Life insurance in such a case is like that of fire and marine insurance,—a contract of indemnity. *Central Nat. Bank vs. Hume*, 128 U. S., 195. The benefit to be gained by death has no periodicity. It is a substitution of money value for something permanently lost, either in a house, a ship, or a life. Assuming, without deciding, that Congress could call the proceeds of such indemnity income, and validly tax it as such, we think that, in view of the popular conception of the life insurance as resulting in a single addition of a total sum to the resources of the beneficiary, and not in a periodical return, such a purpose on its part should be express, as it certainly is not here."

Considering, therefore, the purport of the stipulated facts, considering the uncertainty of Philippine law, and considering the lack of express legislative intention to tax the proceeds of life insurance policies paid to corporate beneficiaries, particularly when in the exemption in favor of individual beneficiaries in the chapter on this subject, the clause is inserted "exempt from the provisions of this law," we deem it reasonable to hold the proceeds of the life insurance policy in question as representing an indemnity and not taxable income.

The foregoing pronouncements will result in the judgment being reversed and in another judgment being rendered in favor of the plaintiff and against the defendant for the sum of P3,148.74. So ordered, without costs in either instance.

Avanceña, C. J., Street, Villamor, Ostrand, Romualdez, Villa-Real, and Imperial, JJ., concur.

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