Republic of the Philippines
COURT OF TAX APPEALS
MANILA

MARIA CARLA PIROVANO,
ESTEBAN PIROVANO and
ESTEFANIA R. PIROVANO,
in the latter's capacity
as Guardian of the minors
ENRICO PIROVANO and
JOHN ALBERT PIROVANO,
Petitioners,

Jan. 31, 1962

C.T.A.
CASES NOS. 347
& 375

- versus -

THE COLLECTOR OF
INTERNAL REVENUE,
Respondent.

x - - - - - - - - - - - x

D E C I S I O N

The petitioners in the above-entitled cases have appealed from the decisions of the respondent holding the former liable for donor's and donees' gift taxes on the alleged donation of the sum of ₱643,000.00 made by the De la Rama Steamship Co., Inc. to petitioners sometime in 1947. In C.T.A. No. 347, petitioners are contesting the legality of the assessment of ₱60,869.67 against each of them, or a total of ₱243,478.68, as donee's gift tax, surcharge and interest. In C.T.A. No. 375, petitioners are seeking the recovery of the sum of ₱34,371.71 as donor's gift tax, while respondent has filed a counterclaim for the sum of ₱18,852.91 as deficiency donor's gift tax, surcharge and interest.

Enrice Pirovano, father of petitioners, was the President and General Manager of De la Rama Steamship Co., Inc. until his death in 1944. Sometime in 1941, the corporation insured the life of Enrico Pirovano with various insurance companies for one million pesos. After the war, the corporation was able to recover from some of the insurance companies the sum of ₱643,000.00 as proceeds of the policies issued on the life of the deceased Enrico Pirovano. By a resolution of the Board of Directors of the corporation dated July 10, 1946, it was proposed "that out of the proceeds of these policies the sum of ₱400,000.00 be set aside for the minor children of the deceased, said sum of money to be convertible into 4,000 shares of stock of the Company, at par, or 1,000 shares for each child." This proposal was modified in another resolution of January 6, 1947, wherein it was resolved that the corporation was to renounce all its rights, title to and interests in said life insurance policies in favor of the children of the deceased; that the proceeds of said policies were to be retained by the corporation in the nature of a loan drawing interest at the rate of 5% per annum from the date of receipt of payments from the insurance companies until paid to said children; and that the corporation would pay the proceeds of said policies to the children of the deceased, plus the corresponding interest, after the corporation shall have settled in full the balance of its bonded indebtedness in the sum of approximately

₱5,000,000.00. Again, in another resolution of June 24, 1947, it was resolved that the annual interest on the proceeds of the policies to be retained by the corporation as a loan from petitioners was to be paid to the heirs of the deceased whenever the corporation was in a position to meet said obligation.

The aforesaid resolutions of the Board of Directors of De la Rama Steamship Co., Inc. were ratified by the stockholders on September 13, 1949, with the modification that "any and all taxes, legal fees, and expenses in any way connected with the above transaction shall be chargeable and deducted from the proceeds of the life insurance policies mentioned in the resolutions of the Board of Directors."

However, on March 8, 1951, the majority stockholders of the corporation revoked the aforesaid resolutions. Accordingly, an action was instituted for the recovery of the balance of the insurance proceeds and the corresponding interest. In G. R. No. L-5377, December 29, 1954, the Supreme Court held the resolutions making the donation valid and ordered the corporation to pay the unpaid balance of the donation to petitioners, together with interest and damages.

Respondent assessed the donor's and donees' gift taxes on the said donation. The corporation paid the donor's gift tax assessed against the corporation in the sum of ₱34,371.71 out of the amount due the petitioners. Contending that the assessments for the donor's and donees' gift taxes are illegal, petitioners have appealed. At the same time, they ask that the sum of ₱34,371.71 be refunded to them.

The main issue relates to the question whether or not the donation in question is a taxable gift. Section 108 of the National Internal Revenue Code provides:

> SEC. 108. Imposition of tax.- (a) There shall be levied, assessed, collected, and paid upon the transfer by any individual, resident or non-resident, of property by gift, a tax, computed as provided in section 109.
>
> (b) The tax shall apply whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible.

The law imposes the gift tax whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible. Thus, for example, a taxable transfer may be effected by the declaration of a trust, the forgiving of a debt, the assignment of a judgment, the assignment of the benefits of a contract of insurance, or the transfer of cash, certificates of deposit or government bonds. (Sec. 86.2, U. S. Treasury Reg. No. 108, cited in Par. 126,131, PH Fed. Taxes, 1955.) Taxable transfers include purported sales of property for less than an adequate and full consideration in money or money's worth, in which case, the amount by which the value of the property exceeds the value of the consideration shall be deemed a gift. (Sec. 111. Revenue Code.)

The donation in question was made by the corporation to the children of the deceased Enrico Pirovano, who left practically nothing to his heirs, out of gratitude for the valuable services rendered by the deceased to the corporation as its President and General Manager. As the donation was made in consideration of the services rendered by the father of petitioners to the corporation, it is alleged that it was a remunerative donation and therefore non-taxable. We quote from the memorandum of counsel for petitioners:

> Considering that the grant or transfer in question was a remunerative donation, being in payment for services rendered, the same does not constitute a taxable gift or donation. For purposes of the gift tax, under the National Internal Revenue Code, a gift or donation is the transfer of property or right without any consideration or for an insufficient or inadequate consideration. "The word 'consideration' means that, when the transferor gives something away and does not at the same time replace it with money of equal value or some goods or services capable of being evaluated in money, he is deemed to have made a gift within the taxing law" (Comm. v. Bristol, 121 F (2d) 129). Services may therefore be a good consideration for transfer of property, and a transfer of property in payment for services rendered cannot be considered a gift for purposes of taxation. (Page 12, Memorandum for Petitioners, Sept. 3, 1959.)

There is no claim or pretense that the deceased Enrico Pirovano was not fully paid for his services, when he was still alive, as President and General Manager of the De la Rama Steamship Co., Inc. Therefore, there was no further obligation on the part of the corporation to pay the deceased or his heirs for such services. As shown by the records, the decision of the Board of Directors of the Corporation and its stockholders to assign all its rights, title to and interests in the insurance policies taken by it on the life of the deceased Enrico Pirovano was motivated solely and exclusively by its sense of gratitude, an act of pure liberality, and not to pay additional compensation for services inadequately paid for. Clearly, the gift is taxable.

Assuming that the gift is taxable, it is contended that the donor corporation is not taxable, the donor's gift tax being imposed only on individuals. (See Sec. 108, Revenue Code, quoted above.) We have passed upon and considered the same question in an earlier case,[1] wherein it was held:

> Section 108 of the Revenue Code was copied from the Federal Gift Tax Law of the United States. The law specifically imposes the donor's gift tax only on individuals. This provision has been interpreted by the U.S. Treasury Department to mean that where

---

[1] St. Stephen's Ass'n. v. Collector, C.T.A. No. 173, May 23, 1959, affd. on another ground in G. R. No. L-15562, May 31, 1961.

a corporation makes a gift, the gift is deemed, for purposes of the Gift Tax Law, to have been made by the individual stockholders and not by the corporation. The U. S. Treasury regulations implementing the Gift Tax Law enumerates examples of taxable gifts, among which is the following:

> "(1) Transfer of property by a corporation to B is a gift to the latter from the stockholders of the corporation. If B himself is a stockholder, the transfer, not being a distribution from earnings or in liquidation to which B is entitled as a stockholder, is a gift to him from the other stockholders." (Sec. 86.2, Regulations 108, U. S. Treasury Department; Par. 126,131, P-H Federal Taxes /1955/.)

This interpretation finds justification in the provision that the tax shall apply whether the gift is direct or indirect. Where a corporation makes a donation, the same is deemed to have been made by the stockholders indirectly through the corporation. In such case, the corporation is not required to file a return or to pay the gift tax. The stockholders are the ones required to file donor's gift tax returns in respect of their individual shares in the donation. (See Joseph P. Crockett, the Federal Tax System of the United States, A survey of Law and Administration, page 78.)

It is argued on behalf of respondent that to interpret the law as not taxing donor corporations would run counter to the purpose of the law which is to prevent avoidance of the estate and inheritance taxes and the income tax, and that such a construction would lead to absurdities.

There is no question that the Law imposing taxes on gifts has for its primary objective to prevent avoidance of the estate, inheritance and income taxes. But when a corporation makes a gift, this purpose is absent. In making a gift, a corporation does not avoid the estate and inheritance taxes because it is not liable therefor. Neither may it make a gift for the purpose of avoiding the income tax, unlike an individual with substantial annual income. Therefore, the purpose of the Gift Tax Law is no argument in favor of the liability of corporations for donor's gift tax.

Section 121 of the Revenue Code has been cited in support of the theory that the law intends to tax corporations making donations. Said section reads:

> SEC. 121. Specific penalties.- (a) Any person required under this Chapter to pay any tax, or required by law or regulations made under authority thereof to make a return, keep any records, or supply any information for the purpose of the computation, assessment, or collection of any tax imposed by this Chapter, who fails to pay such tax, make such return, keep such records, or supply such information, at the time or times required by law or regulations, shall, in addition to other penalties provided for in this Chapter, be fined not more than two thousand pesos or imprisoned for not more than six months, or both.
>
> (b) Any person who attempts in any manner to evade or defeat any tax imposed by this Chapter, or the payment thereof, or who transfers, fictitiously by sale or otherwise any property to evade or defeat the purposes of this Chapter, shall, in addition to other penalties, be punished by a fine of not more than four thousand pesos or imprisoned for not more than one year, or both.

It is argued that if the intention of Congress is to give the word "individual", as used in Section 108, a restricted and literal meaning, it would have used the terms "donor" or "donee", as the case may be, instead of the term "person" in Section 121, since the word "person" is a generic term of comprehensive nature. The use of the term "person" in Section 121 is no indication of an intention to tax corporations as donors. The term "person" in Section 121 can only refer to individuals, because corporations are not liable to imprisonment.

It is said that not to tax corporations would lead to absurdities. In the United States from whose law Section 108 of the Revenue Code was copied verbatim, corporations are not subject to the donor's gift tax. We do not think it would be proper for us to give our law a meaning different from that given to it in the country of origin. If it is desired to give our law a different meaning and application, the remedy is by appropriate legislation.

The other issue raised refers to the legality of the imposition of certain surcharges and interest for failure to file donor's and donee's gift tax returns and for delinquency in the payment of the tax. Since the donor in this case is not subject to the donor's gift tax, we shall consider only the legality of the surcharges and interest on the donees' gift taxes assessed against petitioners.

The surcharge of 25% has been imposed by reapondent for failure of the donees, petitioners herein, to file the corresponding return on or before March 1, 1948, as required by Section 115 of the Revenue Code, pursuant to Section 120 of the same Code, which provides:

> SEC. 120. Ad valorem penalties.- In case of any failure to make and file a return within the time prescribed in subsection (c) of section one hundred fifteen or by the Collector of Internal Revenue, there shall be added to the tax twenty-five per centum of its amount, except that, when a return is voluntarily and without notice from the Collector filed after such time, and if it is shown that the failure to file it was due to a reasonable cause and not to willful neglect, no such addition shall be made to the tax. In case a false or fraudulent return is wilfully made, there shall be added to the tax or to the deficiency tax, in case any payment has been made on the basis of such return before the discovery of the falsity or fraud, a surcharge of fifty per centum of its amount. The amount so added to any tax shall be collected at the same time and in the same manner and as a part of the tax unless the tax has been paid before the discovery of the neglect, falsity, or fraud, in which case the amount so added shall be collected in the same manner as the tax.

Section 120 imposes the 25% surcharge on the tax due where the donee fails to file the necessary return within the time prescribed in Section 115. However, the surcharge may not be imposed if it is shown that the failure to file the return was due to a reasonable cause and not to willful neglect.

In this case, the donation was revoked by majority of the stockholders of the De la Rama Steamship Co., Inc., and it was only after a protracted litigation that the right of petitioners to the donation was settled by final decision of the Supreme Court. Under the circumstances, it is obvious that the failure of petitioners to file the corresponding returns was due to a reasonable cause. In a case involving similar facts under Section 102 of the Revenue Code, this Court held that the said surcharge may not be imposed. To quote from the decision in said case:

> However, we find that the failure of plaintiffs to file an estate and inheritance tax return was due to a reasonable cause. At the time that the return was due, they had not received even a portion of the proceeds of the four insurance policies. In fact, they had every reason to doubt whether they could ever collect under the policies considering that the insurance companies cancelled said policies and refused to pay until after court proceedings were instituted; and in the case of the Philippine American Life Insurance Company, plaintiff Ben L. Chuy was paid only sometime in 1954 after the Supreme Court decided the case in his favor. For this reason, we are of the opinion that the imposition of the 25% surcharge for failure of plaintiffs to file a return for the estate of the deceased Dee So is not in order. (Ben L. Chuy v. Collector, Manila C.C. No. 12823, decided by this Court on July 16, 1958, citing Coll. of Int. Rev. v. Batangas Transp. Co., G. R. No. L-9692, Jan. 6, 1958.)

The other surcharge is the 5% surcharge imposed by Section 119(c) of the Revenue Code, which provides:

> SEC. 119. (c) Surcharge.- If any amount of the taxes included in the notice and demand from the Collector of

> Internal Revenue is not paid in full within thirty days after such notice and demand, there shall be collected in addition to the interest prescribed above and as a part of the taxes a surcharge of five *per centum* of the unpaid amount.

Under the law, if any gift tax is not paid within thirty days after notice and demand by the Commissioner of Internal Revenue, a surcharge of 5% shall be imposed. Petitioners herein failed to pay within said period the gift tax assessed against each of them. Accordingly, the said surcharge has been properly imposed.

With respect to the interest of 1% on the donees' gift tax for delinquency, respondent seeks to justify the liability of petitioners therefor under Section 119(a)(1), which provides:

> SEC. 119. (a)(1) *Payment not extended.* - Where the amount of the taxes determined by the donor or the donee as the taxes or any part of such amount is not paid on the due date of the taxes, there shall be collected as a part of the taxes, interest upon such unpaid amount at the rate of one *per centum* a month from the due date until it is paid.

Pursuant to Section 119(a)(1), respondent is seeking to collect from petitioners interest on the unpaid tax at the rate of 1% a month from the due date until paid. According to respondent, the tax was due on May 15, 1948 as the donation was made in 1947, in accordance with Section 116. On the other hand, petitioners claim that the donation became complete only in 1955 when payments were made by the donor, so that the tax became due only on May 15, 1956. We believe both are incorrect.

The evidence shows that the donation in question was made in 1947 by resolutions of the Board of Directors of the De la Rama Steamship Co., Inc. The insurance proceeds were entered in the books of the Corporation as a loan from petitioners with interest at 5% per annum. In fact, the loan began to draw interest from October 1, 1946. (See 2nd Indorsement of Examiner Francisco E. Testa, Aug. 22, 1960, pp. 38-44, Vol. II, B.I.R. records.) Payments from interest earned were made to plaintiffs from time to time. 750 shares of stock worth ₱150,000.00 in the Denwood Realty Corporation of New York owned by the donor were transferred in the names of petitioners as of December 31, 1949 and charged against the principal of the loan. It is true that the balance of the amount donated was paid in full in 1955, but the facts that the resolutions of the Board of Directors of the donor corporation were made in 1947 and duly accepted in the same year; that the donation was entered in the books of the corporation as a loan from petitioners with the consent of the latter; and that interests on the loan were credited by the donor in favor of petitioners even before the donation was made, show beyond doubt that the donation became complete in 1947 and not in 1955. Since the donation was treated as a loan by the donor, payable at some future time with interest, it is deemed to have been constructively received by the donees from the moment it was recorded in the books of the donor as such loan. Therefore, we agree with respondent that petitioners should have filed donees' gift tax returns not later than March 1, 1948 and paid the tax on or before May 15, 1948. (See Secs. 115(b) and 116(a).)

It appears, however, that no return was filed by the donees pursuant to Section 115(b). Accordingly, the tax assessed by respondent against petitioners is a deficiency tax.

> "The term 'deficiency' means (1) the amount by which the taxes imposed by this Chapter exceed the amount shown as the taxes by the donor or donee upon his return; but the amount so shown on the return shall first be increased by the amounts previously assessed (or collected without assessment) as a deficiency, and decreased by the amounts previously abated, refunded, or otherwise repaid in respect of such taxes; or (2) if no amount is shown as the taxes by the donor or donee upon his return, or if no return is made by the donor or donee, then the amount by which the taxes exceed the amounts previously assessed (or collected without assessment) as a deficiency; but such amounts previously assessed, or collected without assessment, shall first be decreased by the amounts previously abated, refunded, or otherwise repaid in respect of such taxes." (Sec. 122, Rev. Code; emphasis supplied.)

The tax assessed by respondent against each petitioner is, therefore, a deficiency, and the interest collectible for delinquency in the payment of such deficiency is Section 119(b)(1) and not paragraph (a)

(1) thereof, the latter being applicable only to the interest for delinquency in the payment of the tax shown on the return. Section 119(b)(1) provides:

> "Where a deficiency, or any interest assessed in connection therewith, or any addition to the taxes provided for in section one hundred twenty is not paid in full within thirty days from the date of the notice and demand from the Collector (now Commissioner), there shall be collected as a part of the taxes, interest upon the unpaid amount at the rate one per centum a month from the date of such notice and demand until it is paid." (Emphasis supplied.)

It is clear from the foregoing that the interest of 1% a month on a deficiency gift tax is collectible only from the date of notice and demand made by the Commissioner of Internal Revenue upon the taxpayer until the tax is paid, if it is not paid within 30 days from such notice and demand.

In this case, it appears that the assessment, or the notice and demand, was made by respondent on March 8, 1955. (See par. 2, Amended Petition for Review; par. 1, Amended Answer.) The tax has not been paid until now. Therefore, petitioners are liable for the monthly interest of 1% only from March 8, 1955 until the tax is paid.

It is to be noted that the law does not provide for payment of interest on deficiency donor's or donee's gift tax from the due date to the date the deficiency is assessed. On this point, the law governing estate and inheritance taxes is different from the law applicable to gift taxes. In the case of estate and inheritance taxes, Section 100 provides for the collection of interest on the deficiency tax at the rate of 6% per annum from the due date of the tax to the date the deficiency is assessed. No corresponding provision can be found in the Gift Tax Law. In the absence of such or similar provision, no interest is collectible on a deficiency gift tax from the due date of the tax to the date the same is assessed.

In resumé, we are of the opinion that (1) the donor's gift tax in the sum of ₱34,371.76 was erroneously assessed and collected, hence, petitioners are entitled to the refund thereof; (2) the donees' gift taxes were correctly assessed; (3) the imposition of the surcharge of 25% is not proper; (4) the surcharge of 5% is legally due; and (5) the interest of 1% per month on the deficiency donees' gift taxes is due from petitioners from March 8, 1955 until the taxes are paid.

IN LINE WITH THE FOREGOING OPINION, petitioners are hereby ordered to pay the donees' gift taxes as assessed by respondent, plus 5% surcharge and interest at the rate of 1% per month from March 8, 1955 to the date of payment of said donees' gift taxes. Respondent is ordered to apply the sum of ₱34,371.76, which is refundable to petitioners, against the amount due from petitioners. With costs against petitioners in Case No. 347.

SO ORDERED.

Manila, Philippines, January 31, 1962.

ROMAN M. UMALI
Associate Judge

WE CONCUR:

MARIANO NABLE
Presiding Judge

AUGUSTO M. LUCIANO
Associate Judge