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REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

JULIE CARPENTER,
Petitioner,

- versus -

C.T.A. CASE NO. 3098

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

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

11/4/83

D E C I S I O N

Petitioner Julie Carpenter filed with this Court on May 23, 1980 a petition for review praying that respondent Commissioner of Internal Revenue desists from collecting the amount of ₱7,553.76, representing deficiency income tax allegedly assessed against her for the year 1974 and that the warrant of distraint and levy which was issued to enforce the collection thereof be cancelled.

Petitioner is a Filipino citizen, who, in 1974, was the advertising manager of Newsweek and as such received the total amount of ₱55,572.00 as salary and commission for said year. She filed her income tax return on April 15, 1975 showing therein a refundable amount of ₱1,414.91.

Thereafter, respondent's Examiner Edgardo Morales of the Withholding Tax Division, Bureau of Internal

Revenue, under Letter of Authority No. 6063 dated August 14, 1975, conducted an investigation of petitioner's income tax return, and instead of a refundable sum, resulted in a finding of a deficiency income tax in the amount of ₱7,553.76 allegedly due and collectible from petitioner for the year 1974 (pp. 11-12, BIR rec.), computed as follows:

Net Income per return		₱35,206.09
Unallowable deduction and additional income:		
Interest	₱3,153.81	
Representation . . .	9,583.00	
Contributions . . .	1,239.40	
Total disallowance		₱13,976.21
Net income per investigation		₱49,185.10
Less personal exemption		1,800.00
Amount subject to tax		₱47,383.00
Less amount previously assessed . .		12,609.00
Amount of tax withheld		6,989.00
Deficiency tax due		₱ 5,620.00
14% mo. int. from 3-16-75 to 8-30-77		1,933.76
Total amount due & collectibel . . .		₱ 7,553.76

Based on the findings and recommendation of Examiner Morales, respondent Commissioner of Internal Revenue sent a letter of assessment and demand dated October 7, 1977 and requesting petitioner to pay the aforesaid amount of ₱7,553.76. Upon receipt thereof, petitioner, through counsel, protested the assessment in a letter of November 15, 1977 asserting that, under the provision of Section 30 of the National Internal Revenue Code, as amended, she is legally entitled to the deductions she had claimed in the total sum of ₱13,976.21 from her gross income of ₱55,572.00.

It will be shown, however, that as early as December 9, 1977, respondent sent a letter requesting petitioner to "present the papers in support of the deductions claimed at the Withholding Tax Division, Room 208, BIR Bldg., East Triangle, Diliman, Quezon City, on January 12, 1978, between 9:00 and 10:00 o'clock in the morning, x x x x which x x x should not be later than February 13, 1978, "(otherwise,) we (he) will proceed with the collection of the said amount of ₱7,553.76, plus the legal increments in accordance with law." (p. 16, BIR rec.; underscoring ours.) On the same date, December 9, 1977, Revenue Service Chief Leonardo Cabanero, sent back to Examiner Edgardo Morales, the whole docket of petitioner's tax case for reinvestigation.

In a 1st Indorsement of Examiner Morales dated October 29, 1979, he recommended that the original assessment of ₱7,553.76 previously assessed against petitioner be sustained and the collection of the deficiency income tax in question be effected. The 1st Indorsement of Examiner Morales dated October 29, 1979 (p. 22, BIR rec.) is quoted below:

> "1st Indorsement
> October 29, 1979
>
> Respectfully returned to the Chief, Withholding Tax Division, the entire docket bearing on the case of Miss Julie Carpenter, 2021 M. H. del Pilar St., Manila, with the information that <u>a reinvestigation cannot be pursued as subject taxpayer or her or representative were not able to come up with receipts or documents which will support her claimed expenses</u>. Inasmuch as the case has been long overdue, the same is returned with a recommendation that the original assessment be sustained, and that the collection of the income tax liability be effected." (underlining ours)
>
> EDGARDO MORALES
> Examiner"

This 1st indorsement was followed by a 2nd indorsement dated January 14, 1980 of Victor Deoferio, Jr., Revenue Service Chief, Bureau of Internal Revenue, reiterating the immediate collection of said deficiency income tax, and consequently, a warrant of distraint and levy dated April 16, 1980, was later served upon petitioner Julie Carpenter. Hence, this appeal.

The sole issue raised in this instant case is whether or not petitioner Julie Carpenter is entitled to the deductions claimed by her in her income tax return for the year 1974.

To enable one to see the light in the right perspective, respondent Commissioner of Internal Revenue, in his Answer dated September 5, 1980 (p. 38, CTA rec.) to the petition for review stated, among others, that:

> "x x x x x
>
> "5. As petitioner refused, neglected and failed and still continues to refuse, neglect and fail to pay her tax liability, notwithstanding the demand, the issuance and execution of warrants of distraint and levy are in order and proper;
>
> "6. Petitioner was given the chance to present proof that said deductions were actually incurred and paid during the taxable year involved;
>
> "7. The claimed deduction of interest, representation and contribution are not sustained or duly supported by the required evidence;
>
> "8. The assessment against the petitioner in the total sum of ₱7,553.76 was made in accordance with law."

During the hearing of this case on August 1, 1980, petitioner's counsel prayed, in a motion for a writ of injunction, that respondent and/or his agents be restrained from enforcing the warrant of distraint and levy, and not having been objected to by respondent, was granted upon her filing a bond from a surety company of good standing.

With the filing of the bond by taxpayer Julie Carpenter, which was subsequently approved by the Court, the collection of the deficiency income tax for the year 1974 was suspended. During the hearing, petitioner presented receipts and other documents to justify and support her claim of the deductions in controversy.

A. Representation or entertainment expenses in the sum of ₱9,583.00. - It is a cardinal rule in taxation that the "deduction" provision in the tax statutes are acts of legislative grace (Perez vs. Collector of Internal Revenue, CTA Case No. 1707, Feb. 10, 1969, p. 44) and only those expenses which satisfies the legal requirements are allowable. At this point, we quote the treatise of Commissioner Jose Arañas regarding allowable expenses in his book, Commentaries on the National Internal Revenue Code, Volume I, at page 181:

> "(30)(4) - Are all expenses deductible from gross income? - Since the deduction of expenses from gross income is a matter of legislative grace, only those expenses which are expressly provided by law are to be allowed. Generally, however, before an expense is allowed as deduction from gross income, it must satisfy three requirements:
>
> (1) The expense must be both ordinary and necessary;

> (2) The expense must be paid or incurred within the taxable year; and
>
> (3) The expense must be incurred in carrying on a trade or business. (See Gen. Electric (P.I) Inc. vs. Collector of Internal Revenue, CTA Case No. 1117 July 14, 1967)
>
> x x x x x
>
> An expense is ordinary when it is common to incur in the trade or business of the taxpayer. It may vary, depending upon the time, place and circumstances under which it is incurred. x x Also, an expense to be ordinary, must be reasonable in amount. (1955 CCH Fed. Tax Course, par. 403)
>
> x x x x x
>
> An expense is considered necessary if it is appropriate and helpful to the taxpayer's business or occupation. When an expense is called necessary, it is merely distinguished from personal expenditure or from one not pertinent to the business of the taxpayer. (1955 CCH, Fed. Tax Course, par. 403)."

It is obvious that under Section 30 of the National Internal Revenue Code, in order to determine whether expenses for entertainment are deductible, these expenses must meet the requirements for the allowance of ordinary and necessary expenses. These expenses must be so incurred for a purpose which is reasonably connected with the business of the taxpayer. If these expenses were incurred for the entertainment of customers, prospective customers and suppliers of goods and services, the same are properly deductible if it can be shown that these were incurred for the promotion of the business of the taxpayer. However, in the instant case, nowhere can it be found from the receipts of expenses a showing as to who was entertained by petitioner by these expenses and for what occasion these expenses were incurred. These, coupled with the fact that Exhibits B-4, B-5, B-6, B-7 and B-8, purportedly receipts of payment for drinks and foods were undated, there is still that big question as to the year these expenses were actually paid or incurred. (Pp. 74-78, CTA rec.) In this instance, petitioner had patently failed, by not testifying in court, to prove that the amounts appearing thereon indeed represented entertainment expenses in the year in question for her clienteles or customers, or otherwise expenses incurred in order to bring more income, or directly connected in the realization thereof. (John Hicks vs. Coll. of Int. Rev., CTA Case No. 58, Oct. 19, 1955.) The entertainment expenses claimed as deduction in the sum of ₱9,583.00 is, therefore, disallowed.

B. Contributions in the amount of ₱1,239.40. - To be allowed as deduction from gross income, these expenses must meet the following prerequisites:

1. These must have been made to any of the organization mentioned under Section 30(h) of the National Internal Revenue Code;

2. These must not exceed 6% of the taxable net income in case of individuals;

3. These are evidenced by adequate records or receipts.

In this connection, Commissioner Jose Arañas, in his book, The National Internal Revenue Code of 1977, at page 289, citing Section 116 of Revenue Regulations No. 2, has this to say:

> "In connection with the claim for deduction of charitable contributions or gifts, there shall be stated in the returns of income the name and address of each organization to which a gift was made and the appropriate date and amount of the gift in each case. Such contribution or gifts will only be allowed as deductions when the taxpayer attaches to his return the receipt duly signed by the responsible officer of the corporation or association to which the contribution or gift has been paid."

Contributions or gifts to the following organizations under Section 30(h) of the National Internal Revenue Code as amended, are deductible from gross income:

> (h) Charitable and other contributions. - Contributions or gifts actually paid or made within the taxable year to or for the use of the Government of the Philippines or any political

> subdivision thereof for exclusively public purpose, or to domestic corporations or associations organized and operated exclusively for religious, charitable, scientific, athletic, cultural or educational purpose or for the rehabilitation of veterans, or to societies for the prevention of cruelty to children or animals, no part of the net income of which inures to the benefit of any private stockholder or individual to an amount not in excess of six per centum in the case of an individual, and three per centum in the case of a corporation, of the taxpayer's taxable net income as computed without the benefit of this paragraph."

On this particular item of claimed deduction, it appears in the records of this case that petitioner had in fact given gifts or contributions to persons and entities, but apparently not to those mentioned entities for which the contribution or gift is deductible. Moreover, it does not show in the receipts as Exhs. C to C-46 that these were clearly for religious purposes. So that, therefore, looking at these receipts by themselves without more, which were presented as evidence of the claimed contributions or gifts would be very inadequate and deficient to support the charitable contributions in question. Hence, the allowance of the claimed contributions and gifts is hereby denied.

C. Interest on loans in the amount of ₱3,152.81.-

Interest is deductible if and when the following requisites are present and satisfied:

1. There is an indebtedness;

2. The indebtedness is that of the taxpayer;

3. The interest was paid or accrued during the taxable year; and

4. Payment of interest is stipulated in writing. (Per Rev. Reg. No. 78, cited on page 125, CTA rec.)

The prerequisites above stated are simplified by the Internal Revenue Code, thus:

1. That there should be an indebtedness; and

2. That there must be a legal liability to pay interest.

It is noted that in one of the hearings of this case, particularly that which took place on March 3, 1982, when petitioner's counsel presented for marking her documentary evidence consisting of Exhibits A to C-4-6, counsel for respondent manifested that they admitted the genuineness and due execution of all said exhibits except Exhibit A, which represented interest in the amount of ₱3,153.81, the admission of which was deferred until after petitioner shall have presented the "Contract of Sale". Have the contract of sale been presented, the same should have served as a basis for petitioner's claim for the interest deduction. However, petitioner failed to come up and present said "Contract of Sale," for which reason her claim for deduction of interest is hereby disallowed. The certification (Exh. A), presented as evidence to prove interest deductibility, "was not properly identified" thereby rendering said evidence worthless to prove an allowable interest deduction.

WHEREFORE, finding the decision of respondent Commissioner of Internal Revenue imposing a deficiency tax for 1974 in the amount of ₱7,553.71 against petitioner in order, the same is hereby affirmed. With costs against petitioner.

SO ORDERED.

Quezon City, Metro Manila, November 4, 1983.

CONSTANTE C. ROAQUIN
Associate Judge

WE CONCUR:

AMANTE FILLER
Presiding Judge

ALEX Z. REYES
Associate Judge