CONSUELO L. VDA. DE PRIETO,
Petitioner,

- versus - C.T.A. CASE NO. 359

April 22, 1958

COLLECTOR OF INTERNAL
REVENUE,
Respondent.

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D E C I S I O N

This petition for review was filed in connection with an assessment for deficiency income tax made by respondent against petitioner in the sum of ₱21,410.38, together with penalties and monthly interest, due to the disallowance of the latter's claim for deduction of interest paid for late payment of gift taxes on donations she made to her children.

The facts of this case, as stipulated by the parties, follow:

> "1. That petitioner is a Filipino citizen, of legal age, widow and a resident of 137 Aguado, San Miguel, Manila, and that respondent is the duly appointed, qualified and incumbent Collector of Internal Revenue of the Philippines, with principal office at the Finance Building, Manila;
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> "2. That on December 4, 1945, the petitioner conveyed and transferred by way of gifts to her four (4) children, namely, Antonio Prieto, Benito Prieto, Carmen Prieto de Caro, and Mauro Prieto, real property with an assessed value of ₱892,497.50;
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> "3. That the donor's and donee's gift tax returns were filed only on or about February 1, 1954;

"4. That the donor's tax return showed net gifts of ₱892,497.50, and a donor's tax, exclusive of the penalties for late payment, in the sum of ₱52,682.29;

"5. That for gift tax purposes, all the real estate conveyed and transferred by the donor was appraised by the respondent at ₱1,231,268.00, as a result of which the donor's tax, exclusive of the penalties for late payment, was increased to ₱61,697.85, or an increase of ₱9,015.56 over the donor's tax shown in the return;

"6. That on March 24, 1954, the petitioner received assessment notice No. G-A-2787-45, as evidenced by Annex 'A', attached to petitioner's Petition for Review, calling for the payment on or before April 30, 1954, of the total sum of ₱117,706.50, representing the donor's gift tax, interest and compromise, detailed below as follows:

'Donor's gift tax	₱61,697.85
1% monthly interest on ₱52,682.29 from March 1, 1946 to April 30, 1954	51,628.64
1/2% monthly interest on ₱9,015.56 from March 1, 1946 to March 19, 1954	4,350.01
Compromise for failure to file notice of donation	10.00
Compromise for late filing of donor's gift tax return	20.00
Total Tax and Penalties	₱117,706.50'

"7. That the total amount of ₱117,706.50 was paid by the donor, under Official Receipt No. 1524, dated April 29, 1954, as evidenced by Annex 'B', attached to petitioner's Petition for Review;

"8. That of the ₱117,706.50 as total tax and penalties, the sum of ₱55,978.65 represents the total interest collected by the respondent from the petitioner for late payment of the donor's tax;

"9. That in due time, petitioner filed her income tax return covering her income during the year 1954 and that, among the items she claimed as deduction is the total amount of ₱55,978.65 as interest;

"10. That in due course, the income tax return of the petitioner for 1954 was verified by the respondent and as a result of the said verification, the sum of ₱55,978.65, as interest paid by the petitioner in 1954 on account of late payment of the gift tax was disallowed by respondent as evidenced by respondent's letter addressed to petitioner's attorney on February 21, 1957, which was received only on March 6, 1957, as evidenced by Annex 'C', attached to petitioner's Petition for Review;

"11. That as a consequence of the disallowance of ₱55,978.65 by the respondent from the gross income of petitioner for the year 1954, the respondent sent an assessment notice requiring petitioner to pay the sum of ₱19,991.11, as deficiency income tax due on the said sum of ₱55,978.65, together with the 5% surcharge, the 1% monthly interest and the compromise for late payment as detailed below:

'Deficiency tax due on ₱55,978.65	₱19,991.00
5% surcharge	999.55
1% monthly interest from February 4, 1957 to March 31, 1957	379.83
Compromise for late payment	40.00
Total Tax and Penalties	₱21,410.38

"12. That petitioner alleges that the total interest paid by petitioner to the respondent on April 29, 1954 in the sum of ₱55,978.65 incident to late payment of the donor's tax is deductible from her gross income in 1954, under section 30(b) of the National Internal Revenue Code;

"13. That respondent, on the other hand, alleges that the said interest is not deductible from gross income under said section 30(b) of the Tax Code and section 80 of Revenue Regulations No. 2 of the Department of Finance, which provides that 'the word 'taxes' means taxes proper and no deductions should be allowed for amounts representing interest, surcharge, or penalties incident to delinquency';

"14. That both petitioner and respondent admit that the sum of ₱19,991.00 plus the 5% surcharge and 1% monthly interest from February 4, 1957 to the date of payment plus a compromise of ₱40.00 are due from the petitioner if it is decided that the sum of ₱55,978.65 as interest incident to late payment of the donor's tax is not deductible from petitioner's gross income, just as both parties also admit that the said sums are not due from the petitioner if the question is decided affirmatively; and

"15. That both petitioner and respondent submit the question to this Honorable Court for decision."

As stated by the parties, the only issue here is whether or not interest paid by petitioner for late payment of donor's tax is deductible from the gross income of the donor.

Petitioner contends that the interest, incidental to late payment of her gift taxes, is deductible from her gross income under section 30(b) (1) of the National Internal Revenue Code. Respondent, on the other hand, argues that the interest contemplated by section 30(b) (1) of the Tax Code is confined to interest on indebtedness and does not apply to interest on a tax which is allegedly not a debt.

Under the Income Tax Law, there is allowed as deduction from gross income the "amount of interest paid within the taxable year on indebtedness",(section 30(b) (1), National Internal Revenue Code).

The afore-quoted rule requires (a) that there should be an indebtedness, (b) that interest qua interest is paid or accrued thereon, and (c) that what is claimed as an interest deduction should have been paid or accrued within the year. A failure to prove that the item claimed as deductible satisfies these requirements will result in the denial of deductibility (Mertens, Law of Federal Taxation, Vol. 4, Section 26.01, p. 535).

In the case at bar, two requirements are conceded to have been satisfied. Admittedly, the item in question is an interest paid by petitioner in consequence of the late payment of her donor's tax, and the same was paid within the year it is sought to be deducted. The only question that remains to be determined is whether the same was paid upon an indebtedness. In other words, the issue before us hinges upon whether or not the interest paid on the donor's tax is an "interest on an indebtedness" within the contemplation of Section 30(b) (1) of the Tax Code.

To sustain the proposition that the interest payment in question is not deductible for the purpose of computing petitioner's net income, respondent relies heavily on Section 80 of Revenue Regulation No. 2, (known as Income Tax Regulation) promulgated by the Department of Finance, which provides that "the word 'taxes' means taxes proper and no deductions should be allowed for amounts representing interest, surcharge, or penalties incident to delinquency." This provision is identical to that of Section 33 of Regulations No. 20, which interpretative provision, is cited by respondent as authority for his proposition, and which was sanctioned in Anderson v. Posadas, 66 Phil. 205. We find Section 8 of Regulation No. 2 and the interpretative ruling in the Anderson v. Posadas case, supra, to be inapplicable to the issue raised here. It should be noted that petitioner seeks deduction of the interest payment in question as interest on indebtedness, under Section 30(b) (1) and not as taxes, under Section 30(c) (1) (D) of the Tax Code.

The interest here in question was apparently collected from petitioner as donor under Section 118 of the Tax Code. We find, however, no reason why the interest payable by the donor under said Section 118 should be considered as anything other than "interest on indebtedness". In fact, it is characterized by the Tax Code itself as interest. It is graduated with the time the payment of the tax is withheld by the obligor (the delinquent taxpayer). The rate of interest is further fixed either at the normal legal rate of 6% per annum or the maximum rate of 12% per annum. True that for assessment and collection purposes the interest is assessed and collected as part of the tax, nevertheless, it does not form part of the tax itself. If at all the only authority presented by respondent is the regulation that interest is not deductible as a tax. But here the deduction is as interest and no reason or authority has been given which directly prohibits its deduction as interest and we see no basis to deny its deduction as interest especially where the law itself denominates it as such.

The Supreme Court, in the case of Santiago Sambrano vs. Court of Tax Appeals and Collector of Internal Revenue (53 O.G. 4839, No. 15, August 15, 1957), speaks of the nature of taxes thus:

> "Although taxes already due have not, strictly speaking, the same concept as debts, they are, however, obligations that may be considered as such.
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> "'The term 'debt' is properly used in a comprehensive sense as embracing not merely money due by contract but whatever one is bound to render to another, either for contract, or the requirements of the law. (Camben vs. Fink Coule & Coke Co. 61 LRA 584.)
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> "'Where statute impose a personal liability for a tax, the tax becomes, at least in a broad sense, a debt. (Idem)
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> "'A tax is a debt for which a creditor's bill may be brought in a proper case. (State vs. Georgia Co., 19 LRA 485.)'"

From the above pronouncement, a tax may be considered an indebtedness within the contemplation of Section 30(b) (1) of the Tax Code. Consequently, we find that the item of ₱55,978.65, representing interest paid by petitioner for late payment of her donor's tax, satisfies the three conditions precedent to its deductibility under said codal provisions.

The conclusion that the interest paid in the instant case is thusly deductible from the gross income of petitioner finds further support in the jurisdiction from whence our Income Tax Law has been adopted. Thus in the ruling ofthe U. S. Treasury Department, rendered under the Revenue Act of 1918, on provisions substantially similar to ours, it is stated thus,

> "The question arises, however, whether this interest is for all purposes to be regarded as part of the tax. I am of opinion that such is not the intent of the statute. Sections 214 (a) 2 and 234 (a) 2 expressly provided for the deduction from gross income of all interest paid or accrued within the taxable year on the indebtedness of an individual or corporation (with certain specific exceptions). Interest paid under the provisions of section 250 is interest within the meaning of sections 214 (a) 2 and 234 (a) 2, notwithstanding that it is added to the amount of the tax. Had it been intended that interest paid or accrued on income taxes should be excluded from deductions, such exception would have been set forth specifically in sections 214 (a) 2 and 234 (a) 2, as was done in the case of interest on the indebtedness incurred or continued to purchase or carry obligations (other than obligations of the United States issued after September 24, 1917) the interest upon which is wholly exempt from taxation under the income tax.
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> "Sections 214 (a) 3 and 234 (a) 3, Revenue Act of 1918, which provide for the deduction of taxes paid or accrued within the taxable year, expressly except income, war profits, and excess profits taxes. This exception, however, is not intended to include interest payments made under the provisions of section 250. To so hold would amount to a direct contradiction of the provisions of the previous subdivision expressly providing for the deduction of interest.

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"It is held, therefore, that interest paid or accrued under the provisions of section 250, Revenue Act of 1918, is deductible under the provisions of section 214 (a) 2 or section 234 (a) 2 in computing net income." (Law Opinion 922, 2 C.B. 227, reproduced in Toy & Lucas v. Comm. 34 BTA 877, 883.)

This administrative (treasury) opinion that interest paid on taxes is interest on indebtedness and deductible from income has been sustained in several decisions of the U. S. Board of Tax Appeals, Tax Court, District Courts and Circuit Courts of Appeals. (See U.S. vs. Jaffrey, 97 F 2d 488, aff'd 306 US 276; Toy & Lucas v. Comm., 34 BTA 1936 877; Hill v. Comm., 37 BTA 782; Max Thomas Davis v. Comm., 46 BTA 663; Smith v. Comm., 6 T.C. 255; Behl v. Comm., 7 T.C. 1473; Jergens v. Comm., 17 T.C. 806; Penrose v. U.S., 18 F. Supp. 413; Koppers Co. v. Comm., 3 T.C. 62 aff'd 151 F (2d) 267; see also U.S. v. Childs 266 U.S. 304, 307-308; 69 L Ed 299, 300.)

Great weight, at least persuasive if not authoritative, should be given to the construction placed upon the comparable provision by the department (the U.S. Treasury Department) which is charged with the execution of the American counterpart (see Madrigal et al. v. Rafferty, et al., 38 Phil. 414) _Contemporanea expositio est fortissima in lege._ And it is proper in interpreting a statute adopted from another jurisdiction, to consider the interpretation of the act by the courts of the state or country from which it was adopted (50 Am. Jur., sec. 458, pp. 471-472). We therefore find no strong reason that warrants departure from the contemporaneous construction placed by American administrative and judicial authorities upon the deductibility from income of interests incidental to late payment of taxes as "interest on indebtedness".

The concept of "interest on indebtedness", expressed by us in Kuenzle & Streiff, Inc. v. The Collector of Internal Revenue, C.T.A. Case No. 169, July 18, 1956, cannot be advanced in support of respondent's proposition of non-deductibility of the instant interest payment because said conceptual delineation was laid down in view of the particular contractual relationship of the petitioner-corporation and its employees. Consequently, our definition therein was directed to interest on indebtedness arising from contracts. In that case, the claim for deduction was denied because "it does not appear to us that the interest in question had been contracted by petitioner for the use or forbearance of money borrowed from its employees." In other words, in that case, the Court found that there was no indebtedness incurred in which interest was paid or incurred. This situation does not appear in the case at bar. It should therefore be impressed here that interest on indebtedness arising from law is equally entitled to deductibility under Section 30(b) (1) of the Tax Code.

WHEREFORE, the decision appealed from is hereby reversed, without special pronouncement as to costs.

SO ORDERED.

Manila, April 22, 1958.

MARIANO NABLE
Presiding Judge

I CONCUR:

ROMAN M. UMALI
Associate Judge

Associate Judge AUGUSTO M. LUCIANO
on leave.

Affirmed by S.C. in G.R. No. L-13912
Sept. 30, 1960