REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

SECOND DIVISION
****

MARIPOSA PROPERTIES, INC., Petitioner,	**C.T.A. CASE No. 6402**
	Members:
- versus -	**CASTAÑEDA, JR.**, *Chairperson* **UY**, *and* **PALANCA-ENRIQUEZ**, *JJ.*
COMMISSIONER OF INTERNAL REVENUE, Respondent.	Promulgated: FEB 1 3 2007

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DECISION

UY, *J.*:

This is a judicial appeal seeking the cancellation and withdrawal of the assessments issued by the respondent against petitioner for deficiency income tax (P2,615,267.49), value-added tax (P33,223.64), expanded withholding tax (P1,325.41) and documentary stamp tax (P2,402.50) for taxable year 1997 in the aggregate amount of P2,652,219.04.

The Facts

The antecedent facts as borne by the records of this case are as follows:

Petitioner is a domestic corporation duly organized and existing under the laws of the Republic of the Philippines with principal office at PHINMA Plaza, 39 Plaza Drive, Rockwell Center, Makati City.

Respondent, on the other hand, is the duly appointed Commissioner of Internal Revenue, duly authorized to perform the duties of his office, including, among others, the power to decide, cancel and abate tax liabilities pursuant to

Section 204 (B) of the National Internal Revenue Code (NIRC) of 1997 and to enforce the provisions of the Code, with office address at the Fourth Floor, BIR National Office Building, Agham Road, Diliman, Quezon City.

During the year of 1997, petitioner made a series of donations in cash and property totaling P4,500,000.00 to Mariposa Foundation, Inc. (Foundation), a non-stock, non-profit corporation duly organized and existing under and by virtue of the laws of the Philippines, financed and maintained by means of donations and contributions from any persons or entities,[1] and recognized as a qualified donee institution.[2]

On December 7, 1998, respondent issued Letter of Authority No. 138537 authorizing the examination of petitioner's books of accounts and other accounting records for all internal revenue taxes for the period January 1 to December 31, 1997.[3] This Letter of Authority was revalidated on June 15, 2000.

Consequently, on July 1, 2001, petitioner received the letter of respondent of same date, inviting the former for an informal conference to enable the petitioner to go over the findings of the examiner and to submit whatever documentary evidence it may have to support any objection against said findings.[4]

On October 31, 2001,[5] petitioner received from respondent Formal Assessment Notices all numbered LA-138537-97-01-852 and dated October 24, 2001, informing it of the deficiency income tax (P2,615,267.49), value-added tax (P33,223.64), expanded withholding tax (P1,325.41) and documentary stamp tax

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[1] Articles of Incorporation, Exhibit "F".
[2] Certificates of Registration, Exhibits "G" and "H".
[3] Letter of Authority, BIR Records, p. 231.
[4] Paragraph (j), Stipulation of Facts, Rollo, p. 90; Exhibit "2", BIR Records, p. 378.
[5] See Letter-Protest dated November 23, 2001; BIR Records, pp.479-485.

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(P2,402.50) assessments for taxable year 1997 together with the letter of discrepancy, in the aggregate amount of P2,652,219.04.[6]

On November 26, 2001, petitioner, through its external auditor, filed with the respondent's Bureau of Internal Revenue (BIR) its protest letter dated November 23, 2001 contesting the propriety and legality insofar as the subject deficiency income tax assessment issued against it for the taxable year 1997 is concerned. On the other hand, likewise stated in said protest letter, petitioner signified its willingness to pay the amounts of deficiency value-added tax (P33,223.64), expanded withholding tax (P1,325.41) and documentary stamp tax (P2,402.50) assessments for taxable year 1997.[7]

In a letter dated January 30, 2002 from the Regional Director of the Revenue Region No. 8 of the BIR, received on February 4, 2002 by petitioner through its external auditor, petitioner was informed that its request in the protest letter of November 23, 2001 that the issues raised therein be first resolved before the payment of the deficiency taxes attributable to undisputed portion of the deficiency tax assessment was denied for lack of legal and factual basis.[8]

On March 1, 2002, the instant Petition for Review was filed by the petitioner.

In his Answer filed on May 30, 2002, which was admitted by this Court in the Resolution dated July 18, 2002, respondent asserts the following Special and Affirmative Defenses:

> "3. He reiterates and repleads the preceding paragraphs of this answer as part of his Special and Affirmative Defenses;
>
> 4. Section 228 of the (1997) Tax Code, partly provides:

[6] Paragraphs (c), (d) and (k), Stipulation of Facts, Rollo, pp. 89-90.
[7] Paragraphs (e) and (m), Stipulation of Facts, Rollo, pp. 89-90.
[8] Final Decision, BIR Records, p. 522.

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> 'Sec. 228. Protesting of Assessment. – (xxx) Such assessment may be ***protested administratively by filing a request for reconsideration or reinvestigation within thirty (30) days from receipt of the assessment*** in such form and manner as may be prescribed by implementing rules and regulations. Within sixty (60) days from filing of the protest, all relevant supporting documents shall have been submitted; ***otherwise, the assessment shall become final.' (Emphasis supplied)***

Considering the failure of petitioner to submit all relevant supporting documents within sixty (60) days from filing its protest, the assessments have already become final by operation of law;

5. Since the assessments have become final, this Honorable Court has no jurisdiction to act on the instant petition;

6. Assuming that this Honorable Court has jurisdiction over the case, the assessments issued against petitioner for deficiency income tax, value-added tax, expanded withholding tax and documentary stamp tax for taxable year 1997, covered under Final Assessment Notices all numbered LA-138537-97-01-852 all dated October 24, 2001 were made in accordance with law and regulations;

7. Based on the records, petitioner failed to comply with the requirements **under Section 29 (h)(2)(C)(ii) of the 1993 Tax Code** which provides that (in order for a) '*donation made to qualified institutions to be deductible in full, such recipient institutions must utilize the donations not later than the fifteenth day of the third month after the close of the recipient institutions' taxable year in which the donations were received*'. From the foregoing, the claimed deduction of petitioner for donations made to Mariposa Foundation, Inc., in the amount of P4,500,000.00 is not deductible in full since only the amount of P1,296,291.26 was utilized by the foundation as of March 15, 1998. Hence, the amount of P4,323,685.35 should be disallowed as valid deduction from its gross income for taxable year 1997;

8. Petitioner failed to withhold and remit the corresponding withholding tax on commission income payments, hence, the amount of P7,500.00 representing commission expense due should be disallowed as valid deduction from its gross income, pursuant to Section 29 (J) of the Tax Code, as amended, which provides that '*any amount paid or payable which is otherwise deductible from, or taken into account in computing gross income or for which depreciation or amortization may be allowed under this Section, shall be disallowed as a deduction only if it is shown that the tax required to be deducted and withheld therefrom has been paid to the BIR in accordance with this Section, Sections 51 and 74 of the Tax Code*';

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9. Petitioner violated the provision under **Section 29 (a)(1) of the 1993 Tax Code** since per comparison of its Financial Statement for the year 1997 and Alpha List of employees, petitioner overstated the claimed salaries and wages expense, hence, it cannot claimed (sic) the amount of P6,318.00 as valid deduction from its gross income for 1997;

10. Petitioner violates the provision under **Section 100 (a) of the 1993 Tax Code (now Section 106 [A] of the 1997 Tax Code)** since it failed to subject to value-added tax (VAT) the amount of P188,000.00 which is the proceeds derived by petitioner from the sale of its Smile City Homes residential unit;

11. Petitioner failed to subject to the 10% expanded withholding tax rate imposed under Revenue Regulations No. 6-85, the amount of P7,500.00 which represents the discrepancy per comparison of the income payments from petitioner's financial statement as against the Alphalists in the amounts of P15,000.00 and P7,500.00, respectively;

12. Petitioner failed to pay documentary stamp tax due on the lease of its real properties with total lease contracts in the amount of P1,912,320.00, in violation of **Section 194 of the 1997 Tax Code** which provides that '*on each lease, agreement, memorandum, or contract for hire, use or rent of any lands or tenements, or portions thereof, there shall be collected a documentary stamp (tax) of three pesos (P3.00) for the first Two Thousand pesos (P2,000.00), or fractional thereof, in excess of the first Two Thousand pesos (P2,000.00) for each year of the term of said contracts or agreement*'; and

13. All presumptions are in favor of the correctness of tax assessments."[9]

In a Resolution promulgated on September 6, 2002, this Court denied petitioner's Motion for Reconsideration of the Resolution dated July 18, 2002 denying petitioner's Motion to Declare Respondent in Default and therefore, admitted respondent's Answer; hence, the case was set for pre-trial. However, on November 22, 2002, petitioner filed a "Motion to Defer Pre-trial" on the ground that it filed a Petition for Certiorari with the Court of Appeals raising the issue on the propriety of

[9] Answer, Rollo, pp. 44-46.

the Resolution dated September 6, 2002, which this Court granted in its Order dated November 27, 2002.

The Second Division of the Court of Appeals, in two Resolutions dated November 15, 2002 and April 11, 2003, dismissed the aforesaid petition by reasons of deficiencies and for failure to comply with the pertinent Rules on Civil Procedure. Thus, petitioner filed its "Manifestation and Motion" on May 21, 2003 before this Court stating that it has already subscribed to the judgment of the Court of Appeals and moved to set the case for pre-trial. The Court granted said motion and proceeded with the pre-trial conference on June 27, 2003.

As previously manifested by petitioner, it is willing to settle the deficiency assessments except the income tax assessment. Accordingly, on September 12, 2003, petitioner paid the amounts corresponding to the subject deficiency value-added tax, expanded withholding tax and documentary stamp tax.[10] Thus, what remains for determination is the validity of the deficiency income tax in the amount of P2,615,267.49 for taxable year 1997.

During trial, petitioner's Assistant Treasurer, Marilyn A. Silvala, testified to prove that the BIR disallowed the donation of petitioner to Mariposa Foundation in the amount of P4,500,000.00 in cash and shares of stocks; while its witness Rosario M. Garado, Accountant of the Foundation, testified, among others, that the Foundation accepted the said donation and the shares of stocks donated were recorded at its fair market value. Both witnesses identified numerous documents in

[10] BIR Tax Payment Deposit Slips and Payment Forms; Exhibits "C", "D" and "E", inclusive; Rollo, pp. 117-122.

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relation thereto.[11] Respondent, on the other hand, did not present any evidence, but merely marked his documentary exhibits.

Both parties were allowed to file their respective memoranda within thirty (30) days from notice.

However, on September 6, 2004, petitioner, through its new counsel, filed an "Urgent Omnibus Motion"[12] to: (a) re-open case for trial and leave of court to present additional evidence; and (b) to defer submission of memoranda, which was granted in open court and confirmed in the Resolution of October 28, 2004. Therefore, petitioner's witnesses were re-called, and further testified and identified additional documentary evidence.

Finally, in a Resolution dated November 22, 2005, petitioner was deemed to have rested its case. Accordingly, the parties were allowed to file their respective memoranda within thirty (30) days from notice. Only petitioner filed its Memorandum.

Hence, this decision.

The Issues

In their Joint Stipulation of Facts and Issues filed on July 30, 2003, the parties submitted the following issues for this Court's resolution:

> "a) Whether or not the petitioner was furnished in writing of the factual basis for the issuance of the deficiency income tax assessment for the year 1997;
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> b) Whether or not the donation made by petitioner to Mariposa Foundation, Inc. in the amount of P4,500,000.00 should be allowed as deduction from its gross income for the year 1997 pursuant to Section 29 (H)(2)(C)(ii) of the National Internal Revenue Code, as amended;

[11] TSN, Hearing on September 17, 2003.
[12] Rollo, pp. 150-156.

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c) Whether or not the recipient of the above donation, Mariposa Foundation, Inc. has complied with the requirements on the utilization of the aforesaid donation pursuant to Section 29 (H)(2)(C) of the National Internal Revenue Code, as amended, in order that said donation would be considered as allowable deduction of petitioner for 1997; and

d) Whether or not petitioner is liable for deficiency income tax assessment in the amount of P2,615,267.49 for taxable year 1997."

This Court's Ruling

The focal point of the controversy hinges on petitioner's alleged liability for deficiency income tax in the amount of P2,615,267.49 for taxable year 1997 by reason of respondent's disallowance of certain items of expense, to wit: (a) P4,323,685.35 representing donation made to Mariposa Foundation, Inc.; (b) P7,500.00 representing commission expenses; and (c) P6,318.00 representing salaries and wages expenses.

Regarding the first issue which refers to a procedural matter, We deem it apropos to resolve the propriety of the subject formal assessment notices issued against petitioner pursuant to Section 228 of the NIRC of 1997, in relation to Section 3 of Revenue Regulations No. 12-99, relevant portions of which are hereunder respectively quoted:

"**SEC. 228. Protesting of Assessment**. – When the Commissioner or his duly authorized representative finds that proper taxes should be assessed, he shall first notify the taxpayer of his findings: xxx

xxx xxx xxx

The taxpayer shall be informed in writing of the law and the facts on which the assessment is made; otherwise, the assessment shall be void."

"**SEC. 3. Due Process Requirement in the Issuance of a Deficiency Tax Assessment**. – xxx

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> (3.1.4) Formal Letter of Demand and Assessment Notice.- The formal letter of demand and assessment notice shall be issued by the Commissioner or his duly authorized representative. The letter of demand calling for payment of the taxpayer's deficiency tax or taxes shall state the facts, the law, rules and regulations, or jurisprudence on which the assessment is based, otherwise, the formal letter of demand and assessment notice shall be void. The same shall be sent to the taxpayer only by registered mail or by personal delivery. If sent by personal delivery, the taxpayer or his duly authorized representative shall acknowledge receipt thereof in the duplicate copy of the letter of demand, showing the following: (a) His name; (b) signature; (c) designation and authority to act for in behalf of the taxpayer, if acknowledged received by a person other than taxpayer himself; and (d) date of receipt thereof."

Petitioner pointed out that the Formal Assessment Notices all numbered LA-138537-97-01-852, duly received by petitioner on October 31, 2001, failed to state the law and the facts upon which the assessments were based. According to petitioner, it could only speculate and make its best guess on how the provisions of the NIRC of 1993 and 1997 were allegedly violated considering that the basis of the same is couched in a vague language. Thus, petitioner concluded that it was not sufficiently informed of the law and the facts on which the subject assessments were made in violation of the abovementioned provisions and of its right to due process.

After a meticulous review of the records of the case, We cannot sustain petitioner's allegation. If indeed it was not informed of the law and the facts on which the subject assessments were made, it could not have been able to pose verbal or written protest/objection thereto in detail.

As can be gleaned from the records, petitioner was given an opportunity to controvert the findings of the respondent's examiners through an informal conference set for the purpose.[13] As a matter of fact, petitioner's Assistant Treasurer, Marilyn A.

[13] Exhibit "2", BIR Records, p. 378; paragraph (j), Stipulation of Facts, Rollo, p. 90.

Silvala, who was also its witness during the trial proper, attended said conference to manifest petitioner's protest/objection to the subject assessments. Moreover, petitioner admitted that it received the Formal Assessment Notices together with the Details of Discrepancies dated October 24, 2001.[14] The computations/details of discrepancies attached to the Formal Assessment Notices clearly show both factual and legal bases contemplated under Section 228 of the NIRC of 1997, in relation to Section 3 of Revenue Regulations No. 12-99, stating the specific provisions of law from which the assessments were based and the facts on how the amounts of the deficiency taxes were arrived at.

Substantially, the aforesaid details of discrepancies clearly explained in various reasons why the subject donations (P4,323,685.35), commission expenses (P7,500.00) and salaries and wages expenses (P6,318.00) were not allowed as deductions from petitioner's gross income for taxable year 1997. Undoubtedly, petitioner did not merely presume but in fact knew the bases of the assailed assessments because it was able to intelligently protest the same in its letter protest[15] and supplement letter protest[16] dated November 23, 2001 and January 19, 2002, respectively.

It bears stressing that the purpose of Section 228 of the NIRC of 1997 in requiring that "[t]he taxpayer shall be informed in writing of the law and facts on which the assessment is made" is to give the taxpayer the opportunity to refute the findings of the examiner and give a more accurate and detailed explanation regarding the proposed assessment(s).[17] The purpose of the said law having been

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[14] Exhibit "3", BIR Records, p.452; paragraphs (c), (d) and (k), Stipulation of Facts, Rollo, p. 89.
[15] BIR Records, pp. 502-508.
[16] Ibid, pp. 517-519.
[17] Belle Corporation vs. Commissioner of Internal Revenue, CTA Case No. 5930, April 4, 2002.

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served in the instant case, Section 228 of the said Code has been complied with. Therefore, the subject assessments, including the deficiency income tax, issued against the petitioner are not null and void.

Generally, a final assessment is a finding by the respondent that the taxpayer has not paid his correct taxes. The purpose of this assessment is to enable the taxpayer to know the law and the facts on which the assessment is made, and to afford him his right to due process once it is served and received. Its ultimate purpose is to ascertain the amount that a taxpayer should pay. This purpose was accomplished in the present case.

The first issue having been settled, this Court now proceeds to rule on the remaining issues, which being interrelated or intertwined, shall be tackled jointly for convenience and brevity.

As regards the issue of the deductibility of the series of donations made by petitioner to the Foundation, the same primarily devolves upon the proper interpretation of Section 29 (h)(2)(C)(ii) of the NIRC of 1993,[18] which provides:

> "**SECTION 29. Deductions From Gross Income**. – In computing taxable income subject to tax under Sections 21 (a), 24(a), (b) and (c); and 25 (a) (1), there shall be allowed as deductions the items specified in paragraphs (a) to (i) of this section: xxx
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> xxx xxx xxx
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> **(h) Charitable and other contributions**. – **(1)** In general. – Contributions or gifts actually paid or made within the taxable year to, or for the use of the Government of the Philippines or any of its agencies or any political subdivision thereof for exclusively public purposes, or to domestic-corporations or associations organized and operated exclusively for religious, charitable, scientific, youth and sports development, cultural or educational purposes or for the rehabilitation of veterans, or to social welfare institutions, no part of the net income of which inures to the benefit of any private stockholder or

[18] Now Section 34 (H)(2)(c)(2) of the NIRC of 1997. Please note that all reference to the term "private foundation" has been replaced by "nongovernment organization".

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individual in an amount not in excess of 6% in the case of an individual, and 3% in the case of a corporation, of the taxpayer's income derived from business as computed without the benefit of this and the following subparagraphs.

(2) Contributions deductible in full. – Notwithstanding the provisions of the preceding subparagraph, donations to the following institutions or entities shall be deductible in full:

xxx xxx xxx

(C) Donations to certain private foundations. — The term "private foundation" means a non-profit domestic corporation:

(i) Organized and operated exclusively for scientific, research, educational, character-building and youth and sports development, health, social welfare, cultural or charitable purposes, or a combination thereof, no part of the net income of which inures to the benefit of any private individual;

(ii) <u>Which, not later than the 15th day of the third month after the close of the foundation's taxable year in which contributions are received, makes utilization directly for the active conduct of the activities constituting the purpose or function for which it is organized and operated, unless an extended period is granted by the Secretary of Finance in accordance with the rules and regulation to be promulgated</u>;

(iii) The level of administrative expense of which, shall on an annual basis conform with the rules and regulations to be prescribed by the Secretary of Finance but in no case to exceed thirty percent (30%) of total expenses; and

(iv) The assets of which in the event of dissolution would be distributed to another non-profit domestic corporation organized for similar purpose or purposes, or to the State for public purpose, or would be distributed by a court to another organization to be used in such manner as in the judgment of said court shall best accomplish the general purpose for which the dissolved organization was organized.

Subject to such terms and conditions as may be prescribed by the Secretary of Finance, the term "utilization" means:

(i) Any amount in cash or in kind (including administrative expenses) paid or utilized to accomplish one or more purposes for which the private foundation was created or organized.

(ii) Any amount paid to acquire an asset used (or held for use) directly in carrying out one or more purposes for which the foundation was created or organized.

An amount set aside for a specific project which comes within one or more purposes of the foundation may be treated as a utilization, but only if at the time such amount is set aside, the private foundation establishes to the satisfaction of the Commissioner of Internal Revenue that the amount will be paid for the specific project within a period to be prescribed in regulations to be promulgated by the Secretary of Finance, but not to exceed 5 years, and the project is one which can be better accomplished by setting aside such amount than by immediate payment of funds." *(Underscoring Ours)*

It is evident that the deductibility of donation is not governed by the ordinary rules on deductibility of an expense as provided for under Section 39 of the NIRC of 1993 [now Section 45 of the NIRC of 1997]. Donation is recognized as a deduction from gross income in the year such donation was actually paid or made, pursuant to the provisions of Section 29(h) of the NIRC of 1993 [now Section 34(H) of the NIRC of 1997]. In other words, "[i]t can be inferred from the foregoing law that donation must be both perfected and consummated before it can be allowed as an expense. Irrespective of the accounting method used, contributions or gifts are deductible only from petitioner's gross income in the year they were actually paid or made".[19]

In the case at bench, the series of donations made by petitioner to the Foundation in the year 1997 amounting to P4,500,000.00, comprise of cash as evidenced by various Certificates of Donations and official receipts[20] issued by the latter and of personal property in the form of shares of stock under the Deed of Donation dated August 25, 1997.[21] A perusal of said documentary evidence shows

[19] Philippine Stock Exchange, Inc. vs. Commissioner of Internal Revenue, CTA Case No. 5995, October 15, 2002.
[20] Exhibits "K" to "DD", inclusive.
[21] Exhibit "I".

that the series of donations were actually perfected and consummated within the year 1997. Thus, said deductions may be claimed as deduction from gross income.

Corollary thereto, BIR-NEDA Regulations No. 1-81, as amended, in implementing the abovequoted Section,[22] provides:

> "**SEC. 2. *Definitions*.** – In these REGULATIONS unless the contrary intention appears, the following terms:
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> xxx xxx xxx
>
> F. 'Private foundation' means a non-profit Domestic Corporation or Association organized and operated exclusively for scientific research, education, character building and youth sports development, health, social welfare, cultural or charitable purpose or a combination thereof, no part of the net income of which inures to the benefit of any private individual.
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> xxx xxx xxx
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> R. 'Utilization by a qualified donee' means –
>
> (a) Any amount in cash or in kind (including administrative expenses) paid or utilized to accomplish one or more purposes for which it was created or organized; or
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> (b) Any amount paid to acquire an asset used (or held for use) directly in carrying out one or more purposes for which the donee was created or organized; or
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> (c) Any amount set aside for a specific project subject to the conditions provided for under Section 9 of the regulations; or
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> (d) Any amount in cash or in kind invested in any activity related to the purpose for which it was created or organized.[23]
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> **SEC. 3. *Conditions for Deductibility*.** –
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> xxx xxx xxx

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[22] As amended by Batasan Pambansa Blg. 45.
[23] As amended by Revenue Regulations No. 10-82 after amendments by BIR-NEDA Regulations No. 1-82.

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B. *Full Deductibility.* – All donations in cash or in kind except personal sources, given to the following institutions or entities shall be deductible in full for income tax purposes;

(a) xxx;

(b) xxx;

(c) Private Foundation which:

(i) Is duly registered with the SEC and governed by trustees who received no compensation nor any type of remuneration in cash or in kind;

(ii) Not later than the 15th day of the third month after the close of the foundation's taxable year in which contributions are received, makes utilization directly for the active conduct of the activities consistent with the purpose or function for which it is organized and operated, unless an extended period is granted by the Minister of Finance not exceeding thirty (30) days in accordance with these rules and regulations;

(iii) The level of administrative expenses on an annual basis does not exceed 30% of its total utilization during the taxable year;

(iv) xxx"

"***SEC. 9. Utilization Requirements.*** –

xxx xxx xxx

B. *For private foundations.*

(a) *Administrative expenses.* – Administrative expenses shall not exceed 30% of total donations for the taxable year.

(b) *Approval requirements for amounts set aside.* – Amounts set aside or to be set aside for a specific project must have the prior approval of the Commissioner of Internal Revenue in writing. Application therefor must contain the following:

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(i) The nature and purpose of the specific project and the amount programmed therefor;

(ii) A detailed description of the project, including estimated costs, sources of any future funds expected to be used for completion of the project, and the location or locations (general or specific) of any physical facilities to be acquired or constructed as part of the project; and

(iii) A statement by an authorized official of the corporation or association that the amount to be set aside will actually be disbursed for the specific project within five years from the date of the approval of the Commissioner of Internal Revenue, pursuant to paragraph (b) hereof unless the nature of the project is such that the five-year period is impracticable.

(c) *Evidence of an amount set aside.* – Amounts set aside shall be evidenced by book of entries and documents showing evidence of deposits or investments, or other documents that the Commissioner may require."[24] *(Underscoring Ours)*

From the foregoing, all donations, in cash or in kind, given to a private foundation or nongovernment organization, are deductible in full for income tax purposes, provided the following requisites are complied with:

1) The private foundation/nongovernment organization must be duly registered with the Securities and Exchange Commission (SEC) to be a qualified donee;

2) The private foundation/nongovernment organization must utilize such donations/contributions in any of the manner provided for in Section 2 (R), paragraphs (a) to (d) of BIR-NEDA Regulations No. 1-81, as amended;

3) Such utilization must be made not later than the fifteenth (15th) day of the third (3rd) month after the close of the foundation's taxable year in which donations/contributions are received

[24] As amended by BIR-NEDA Regulations No. 1-82.

unless extended by the Minister of Finance for a period not exceeding thirty (30) days; and

4) The level of administrative expenses on an annual basis does not exceed thirty (30%) percent of the private foundation's/nongovernment organization's total utilization during the taxable year.

Anent the first requisite, there is no doubt that the Foundation is a duly registered private foundation. Petitioner presented the Foundation's Articles of Incorporation,[25] together with the Certificates of Registration[26] issued by the BIR, showing that it is indeed a private foundation defined under Section 29 (h)(2)(C)(i) of the NIRC of 1993 and Section 2(F) of BIR-NEDA Regulations No. 1-81, as amended.

As the regards the second, third and fourth requisites, petitioner presented a schedule[27] consisting of five (5) pages showing the alleged utilization by the Foundation of the subject donations/contributions during the years 1997 to 2000. Particularly, it submitted numerous documents[28] to establish that the total amount of P1,078,741.00 has in fact been utilized by the Foundation in the year 1997 to accomplish one or more purposes or to invest in any activity related thereto for which it was created or organized.

On March 15, 1998, being the fifteenth (15th) day of the third (3rd) month after the close of the Foundation's taxable year in which the subject donations/contributions were received, petitioner admitted that only the amount of P1,296,291.26 from the total donation of P4,500,000.00 was utilized. However, it argues that the term "makes utilization" contemplated under Section 29 (h)(2)(C)(ii) of the NIRC of 1993, in relation to Section 3 (B)(c)(ii) of BIR-NEDA Regulations No.

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[25] Exhibit "F",
[26] Exhibits "G" and "H".
[27] Exhibits "B" to "B-4"; Rollo, pp. 112 -116.
[28] Exhibits "RRRRRRRRRR" to "KKKKKKKKKKKK-1", inclusive.

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1-81, as amended, does not require that the entire amount of donation be fully disbursed in the succeeding year in order for the donation to be deductible in full from the donor's gross income. Hence, petitioner believes that, as long as the donee institution makes initial disbursements or payments of "any amount" forming part of the donation, the donee is deemed to have made utilization of said donation.

We agree with petitioner's contentions.

Section 29 (h)(2)(C)(ii) of the NIRC of 1993, in relation to Section 3 (B)(c)(ii) of BIR-NEDA Regulations No. 1-81, as amended, clearly provides that a private foundation/nongovernment organization shall, <u>not later than the fifteenth (15th) day of the third (3rd) month after the close of its taxable year in which contributions are received, make utilization of said contributions directly for the active conduct of the activities constituting the purpose or function for which it is organized and operated</u>. The law does not require full payment or utilization of the donations/contributions it received. As long as a portion of such donations/contributions was proven to be utilized in any of the manner provided for in Section 29 (h)(2)(C) of the NIRC of 1993 and Section 2 (R), paragraphs (a) to (d) of BIR-NEDA Regulations No. 1-81, as amended, it may be deducted in full from the donor's gross income.

However, it bears stressing that, BIR-NEDA Regulations No. 1-81, as amended, enumerates the procedures and requirements for the deductibility or the non-deductibility of donations in general:

> "***SEC. 11. Verification procedure and substantiation requirements.***
>
> A. *<u>For Donors</u>*. – Donors claiming deduction from their taxable income for donations authorized by Batasan Pambansa Blg. 45 <u>should submit evidence of the BIR showing submission of the Certificate of Donation and/or Notice of Donation</u>.

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(a) Actual receipt by the donee of the donation and the date of receipt thereof; and

(b) The amount of the donation, if in cash; if real property, the value thereof at the time of the donation, which shall be based on the assessors' most recent valuation; and if personal property had already been used at the time of donation, the depreciated or book value thereof.

B. *For Donees*. – Donees shall include in their income tax return an annual information report with the BIR, *Provided*, that donees covered by the national priority plan, must furnish the NEDA with the annual information report by accomplishing NEDA Forms 3A, 3B and 3C. The report shall be certified by the authorized official of the Institution or Association and shall contain:

(a) A list of the donations and income received during the year, showing the name and address of the donor; the source of income; the amount or market value of each donation and items of income and the disposition thereof;

(b) A list of the activities and/or project undertaken by the institution and the cost of each undertaking indicating in particular where and how the donation has been utilized;

(c) A list of projects; their corresponding costs; the amount 'set aside' and the status of funds balances at the end of the year;

(d) That the utilization requirements under Section 9 of these Regulations have been sufficiently complied with;

(e) That no part of its net income inures to the benefit of any private stockholder or individual." *(Underscoring Ours)*

A careful review of the records shows that neither the Foundation's income tax return and audited financial statements, nor the annual information report duly certified by the authorized official of the Foundation containing the above-enumerated information, was ever presented or submitted by petitioner in this case.

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Although petitioner may have substantially complied with the substantiation requirements for the donors,[29] it however miserably failed to establish that the Foundation has been complying with the substantiation requirements for the donees.

The significance of the aforesaid requirements is further bolstered by the fact that in the Foundation's Certificates of Registration dated October 29, 1993 and January 10, 2002, submission of its Annual Information Return with the lists of donations and income received, activities and/or projects undertaken, projects and amounts set aside, among others, is one of the terms and conditions[30] to be complied with in order to entitle the donor (petitioner) to full deduction and the donee (Foundation) to exemption from donor's tax pursuant to the applicable provisions of the law. In view of the foregoing considerations, this Court is constrained to deny petitioner's claim for the deduction of its series of donations for its failure to establish with clear and convincing evidence that the Foundation complied with the substantiation requirements set forth in Section 11 (B) of BIR-NEDA Regulations No. 1-81, as amended.

In addition, neither an alleged Resolution[31] issued by the Foundation's Board of Trustees nor an express provision in the Foundation's Articles of Incorporation[32] could establish that the level of its administrative expenses on an annual basis did not exceed thirty (30%) percent of its total utilization during the subject taxable year. Again, the same information should have been included in the Foundation's Annual Income Tax Return/Annual Information Report for purposes of the donor's full

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[29] By presenting Certificates of Donations and official receipts issued by the Foundation; Exhibits "K" to "DD", inclusive.
[30] As set forth on the reverse side of Exhibits "G" and "H"; Records, pp. 271-272.
[31] Exhibit "A-1"; Rollo, p. 111 (as contained in the Secretary's Certificate, Exhibit "A").
[32] *Supra*, Article EIGHT; Rollo, p. 268.

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deduction and the donee's exemption from donor's tax. Hence, We could not verify such allegation.

On the remaining matters raised by petitioner in its administrative protest and Petition for Review, particularly those pertaining to the disallowance of commission expenses and salaries and wages expenses in the amounts of P7,500.00 and P6,318.00, respectively, this Court agrees with respondent in disallowing the same as deductions considering that there are discrepancies between the amounts stated in the Alphalists and in the Financial Statements submitted by petitioner. Petitioner should have at least explained why such discrepancies exist and attempted to reconcile the same in order to be allowed as a valid deduction from its gross income. Unfortunately, it failed to do so.

It is settled that deductions are construed strictly against the taxpayer claiming it. He who claims a deduction must point to the specific provision of the statute authorizing it, and he must be able to prove that he is entitled to it. As a general rule, deductions are strictly construed against the taxpayer claiming them and it is incumbent upon the taxpayer to establish a clear right to tax exemption. Tax exemptions are looked upon with disfavor.[33]

Furthermore, the Court notes that although the Assessment Notice[34] issued against petitioner for deficiency income tax for the year 1997 recommended for a 25% surcharge, it failed to include the same. Thus, it must be modified to include a 25% surcharge pursuant to Section 248 of the NIRC of 1997, in addition to the income tax due.

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[33] V. C. Mamalateo, Philippine Income Tax, First Ed., 2004, p.173 (citing Western Minolco Corporation vs. Commissioner of Internal Revenue, 124 SCRA 121 [1983]).
[34] BIR Records, p. 455.

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Likewise, a 20% delinquency interest[35] shall also be included accruing from February 4, 2002, the day petitioner received respondent's Final Decision[36] demanding the payment of the assessed deficiency income tax. Accordingly, the subject deficiency assessment shall be recomputed as follows:

Taxable Income Per Return			P 1,377,155.00
Add:	Discrepancies Per Audit		
	Donations and Contributions	P 4,323,685.35	
	Commission	7,500.00	
	Salaries and Wages Expense	6,318.00	4,337,503.35
Taxable Income Per Audit			P 5,714,658.35
Income Tax Rate			35%
Income Tax Payable Per Audit			P 2,000,130.42
Less:	Tax Paid Per Return		482,004.00
Tax Still Due Thereon			P 1,518,126.42
Add:	20% Interest (04-16-98 to 11-26-01)		1,097,141.07
	25% Surcharge		379,531.61
TOTAL AMOUNT DUE			**P 2,994,799.10**

WHEREFORE, the subject Petition for Review is hereby **DISMISSED** for lack of merit. The assailed Decision of the Commissioner of Internal Revenue dated January 30, 2002 is hereby **AFFIRMED** with some modifications.

Accordingly, petitioner is **ORDERED TO PAY** respondent the amount of **TWO MILLION NINE HUNDRED NINETY FOUR THOUSAND SEVEN HUNDRED NINETY NINE PESOS and 10/100 (P2,994,799.10)** representing deficiency income tax for the taxable year 1997, plus 20% delinquency interest per annum from February 4, 2002 until such time the said amount is fully paid.

SO ORDERED.

ERLINDA P. UY
Associate Justice

[35] Sec. 249 of the NIRC of 1997.
[36] BIR Records, p. 522; Annex "G", Petition for Review.

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WE CONCUR:

JUANITO C. CASTAÑEDA, JR.
Associate Justice

OLGA PALANCA-ENRIQUEZ
Associate Justice

ATTESTATION

I attest that the conclusions in the above Decision were reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

JUANITO C. CASTAÑEDA, JR.
Associate Justice
Chairperson

CERTIFICATION

Pursuant to Article VIII, Section 13 of the Constitution, and the Division Chairperson's Attestation, it is hereby certified that the conclusions in the above Decision were reached in consultation before the case was assigned to the writer of the opinion of the Court.

ERNESTO D. ACOSTA
Presiding Justice

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