REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

PHILIPPINE CASINO OPERATORS CORPORATION,
Petitioner,

- versus -

C.T.A. CASE NO. 4341

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

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

PROVIDENT INTERNATIONAL RESOURCES CORPORATION,
Petitioner,

- versus -

C.T.A. CASE NO. 4342

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:
APR 12 1995

x - x

DECISION

These are consolidated cases involving assessments of alleged deficiency income taxes, 25% surtax of improper accumulation of profits and business taxes for taxable years 1981 to 1985 based on the Memorandum Report (Exh. 3, pp. 230-244, BIR Records) of Mr. Aureliano G.

Sison, Jr., respondent's Supervising Revenue Enforcement Officer, computed as follows:

(Philippine Casino Operators Corporation)

Year	Kind of Tax	Amount	(BIR Rec. Page No.)
1981	Income Tax	P 20,120,627.10	(339-340)
1982	Income Tax	24,694,116.30	(339-340)
1983	Income Tax	24,441,146.10	(339-340)
1984	Income Tax	25,666,646.30	(343-344)
1985	Income Tax	23,502,597.28	(343-344)
		P 118,425,133.08	

Year	Kind of Tax	Amount	(BIR Rec. Page No.)
1981	25% Surtax on Improperly Accumulated Profits	P 2,933,159.75	(339-340)
1982	25% Surtax on Improperly Accumulated Profits	3,598,614.75	(339-340)
1983	25% Surtax on Improperly Accumulated Profits	5,410,797.50	(341-342)
1984	25% Surtax on Improperly Accumulated Profits	6,198,579.00	(341-342)
1985	25% Surtax on Improperly Accumulated Profits	6,333,994.00	(341-342)
		P 24,475,145.00	

1981	Fixed and Percentage Taxes	P 2,689,309.50	(357)
1982	Fixed and Percentage Taxes	2,992,156.44	(355)
1983	Fixed and Percentage Taxes	3,375,817.69	(353)
1984	Fixed and Percentage Taxes	3,980,718.19	(351)
1985	Fixed and Percentage Taxes	4,431,563.59	(348)
		P 17,469,565.41	

286

(Provident International Resources Corporation)

Year	Kind of Tax	Amount	(BIR Rec. Page No.)
1981	Income Tax	P 1,033,743.90	(335-356)
1982	Income Tax	5,729,283.00	(335-336)
1983	Income Tax	5,456,570.70	(335-336)
1984	Income Tax	9,770,685.60	(337-338)
1985	Income Tax	16,577,904.30	(337-338)
1986	Income Tax	20,796,908.00	(332-334)
		P59,365,095.50	
1981	25% Surtax on Improperly Accumulated Profits	P 155,967.88	(335-336)
1982	25% Surtax on Improperly Accumulated Profits	839,181.50	(335-336)
1983	25% Surtax on Improperly Accumulated Profits	1,213,527.25	(332-334)
1984	25% Surtax on Improperly Accumulated Profits	2,364,076.00	(332-334)
1985	25% Surtax on Improperly Accumulated Profits	4,469,881.00	(332-334)
1986	25% Surtax on Improperly Accumulated Profits	6,340,000.00	(332-334)
		P 15,382,633.63	

Year	Kind of Tax	Amount	(BIR Rec. Page No.)
1982	Fixed Tax	P 9,674.85	(359)
1983	Fixed Tax	8,774.85	(359)
1984	Fixed Tax	7,874.85	(359)
1985	Fixed Tax	6,974.85	(359)
1986	Fixed Tax	6,074.85	(359)
		P 39,374.25	
1981	Documentary Stamp Tax	P 22,300.00	(330-331)

On May 8, 1987, petitioners protested the above assessments but was subsequently denied by the respondent in a letter, dated January 3, 1989, (Exh. HH) "since your clients, PIRC and PCOC failed to register and affiliate their businesses with PAGCOR, they are not therefore, entitled to the enjoyment of the tax exemption privileges provided for under Section 13 (2)(e) of P.D. No. 1869." (Emphasis supplied). Apparently, this is the only ground for the denial of said protests.

Hence, these appeals.

In their Petitions for Review, petitioners contended that under Presidential Decree Nos. 1399 and 1869, they are exempt from all taxes, fees or levies of any kind and that registration and affiliation with the Philippine Amusement and Gaming Corporation (PAGCOR) was not needed for them to be tax exempt. But even if registration was not a prerequisite to petitioner's tax exemption, they, however, registered just the same.

Respondent, on the other hand, argued that "Under Presidential Decree No. 1869, in order that corporations, associations, agencies or individuals having any contractual relationship with the PAGCOR in connection with the operation of casinos may be entitled to exemption from taxes, they must register and affiliate their businesses with PAGCOR." (Emphasis supplied; Answer, p. 31 CTA Records) and since petitioners did not register and affiliate their businesses with PAGCOR, they are not entitled to said tax exemption. Moreover, "the tax exemption under P.D. Nos. 1399 and 1869 does not include the 25% surtax on improper accumulation of

288

profits since the surtax is not a tax but a penalty" (ibid.).

The issues to be resolved are:

1) Whether or not registration and affiliation with PAGCOR are required in order that entities having contractual relationship with PAGCOR can claim tax exemption.
2) Whether or not said tax exemption covers surtax on improperly accumulated profits.

We find both issues for the petitioner.

It was not disputed that petitioners, Philippine Casino Operators Corporation (PCOC) and Provident International Resources Corporation (PIRC), had contractual relations (Exhs. A and D for PCOC's Contract to Operate and Exhs. B, C, and E for PIRC's Contracts of Leases) with the PAGCOR. It was also not disputed that under P.D. Nos. 1399 and 1869, PAGCOR was exempted from any kind or form of tax, except a franchise tax of 5% of the gross revenues derived by PAGCOR. Such exemption was also extended to those entities having "contractual relationship in connection with the operations of the casino/s..." Thus, Section 4 (2)(b) of P.D. No. 1399 provided:

> "(b) Others: The exemption herein granted for earnings derived from the operations conducted under the franchise, specifically from the payment of any tax, income or otherwise, as well as any form of charges, fees

> or levies, <u>shall inure to the benefit of and extend to corporation/s, associations/s, agency/ies, or individual/s with whom the Franchisee has any contractual relationship in connection with the operations of the casino/s authorized to be conducted under the franchise and to those receiving remuneration from the Franchise Holder as a result of essential facilities furnished and/or technical services rendered to the Franchise Holder</u>." (Emphasis supplied)

Said exemption was reiterated under Section 13 (2)(b) of P.D. No. 1869 (which consolidated and amended P.D. Nos. 1067-A, 1067-B, 1067-C, 1399 and 1632, relative to the franchise and powers of the PAGCOR) which provided, thus:

> (b) Others: The exemption herein granted for earnings derived from the operations conducted under the franchise specifically from the payment of any tax, income or otherwise, as well as any form of charges, fees or levies, <u>shall inure to the benefit of and extend to corporation(s), associations(s), agency(ies), or individual(s) with whom the Corporation or operator has any contractual relationship in connection with the operations of the casino(s) authorized to be conducted under the Franchise and to those receiving compensation or other remuneration from the Corporation or operator as a result of essential facilities furnished and/or technical services rendered to the Corporation or operator.</u> (Emphasis supplied)

The bone of contention, however, as raised by the respondent lies in the sixth "whereas" clause of P.D. No. 1869 which stated, thus:

> **WHEREAS**, in order to make PAGCOR's regulatory powers more effective, <u>it is necessary that businesses primarily engaged in gambling operations be affiliated with PAGCOR</u>, and become subject to its regulatory powers

298

> with respect to operation, capitalization and organizational structure; (Emphasis supplied).

and in Section 9 of the same decree, thus:

> **Sec. 9.** *Regulatory Power.* - The Corporation shall maintain a Registry of the affiliated entities, and shall exercise all the powers, authority and responsibilities vested in the Securities and Exchange Commission over such affiliated entities mentioned under the preceding section... (Emphasis supplied)

which now form the basis for respondent's assessments against the petitioners. Respondent interpreted that "since the aforesaid entities are required to register and affiliate their businesses with the PAGCOR, it necessarily follows that the tax exemption of the PAGCOR extends to them only if they register and affiliate their businesses with the PAGCOR. This is so because it is the cardinal rule that tax exemptions are not presumed; that they are construed strictissimi juris against the taxpayer and liberally in favor of the taxing authority; that the tax exemption cannot be made by inference or implication but must be proven beyond reasonable doubt and in case of doubt, the same shall be resolved against exemption. xxx" (Respondent's Memorandum, p. 276, CTA Records)

We disagree.

We find such interpretation contrary to reason and common sense, if not, unfair to the petitioners. The use

291

by the respondent of the phrase "they (tax exemptions) are construed <u>strictissimi juris</u> against the taxpayer and liberally in favor of the taxing authority" is to Our mind, very partial to the respondent and obviously prejudicial to the interests of the petitioners. It certainly lacks the required candor in the interpretation of laws. Well-settled is the rule that interpretation of tax laws should be "construed against the Government because revenue laws impose special burdens" (Marinduque Mines Agents, Inc. vs. Hinabangan, Samar, L-18924, June 30, 1964; Luzon Stevedoring vs. Trinidad, 43 Phil 803). If the "intent to tax is clear" which is absent in this case, then the pendulum swings to the other end to favor the government and the oft-quoted rule that "tax exemptions are construed <u>strictissimi juris</u> against the taxpayer" would then govern (see Jai-alai Corp. vs. Collector, 57 O.G. 2490; Commissioner vs. Filipinas Cia de Seguros, L-14880, April 29, 1960).

It would certainly be stretching too far the imagination of this Court in order to find a connection between the "whereas" clause together with Sec. 9 of P.D. 1869 and Sec. 13 (2)(b) of the same decree. There simply is no link between "registration" and "tax exemption". In fine, We find that registration was never intended by

292

law to be a prerequisite for the tax exemption. Otherwise, it would have said so. We agree with the petitioners' observation that "if it had indeed been the intention that registration was a prerequisite for exemption, then Section 13 (2)(b) would have so stated, just as Section 18 of P.D. No. 66, granting enterprises that registered with the Export Processing Zone Authority exemption from certain local taxes and licences. Thus, said law expressly makes the tax exemption available only to a "zone registered enterprise"' (Petitioners' Memorandum, p. 249, CTA Records). In this particular case the law is crystal clear on this matter and leaves no room for interpretation. We are not inclined to confuse the same in an aimless way by responding to respondent's biased interpretation. "Where the law does not distinguish, We ought not to distinguish."

We also find meritorious the other facts and arguments raised by the petitioners, more particularly, that "petitioners have registered with PAGCOR" (Exh. T) and that "assuming registration was necessary, P.D. No. 1869 has no retroactive effect" since said law took effect fifteen days following December 26, 1983, the date of publication in the Official Gazette (Exh. II).

293

Therefore, further discussion on these factual matters and arguments would only be an exercise in verbosity.

As to the other issue raised by the respondent that "tax exemption does not cover surtax on improperly accumulated profits since the surtax is not a tax but a penalty" is again unmeritorious.

Section 13 (2)(b) of P.D. 1869 is also clear regarding petitioners' exemption "from the payment of **ANY** tax, income or otherwise, as well as any form of charges, fees or levies, shall inure to the benefit of and extend to corporation(s), association(s), agency(ies) or individual(s) with whom the Corporation or operator has any contractual relationship..." (Emphasis supplied). The language used in the law is so exhaustive, clear and all embracing that it leaves no room for interpretation other than the petitioners being exempted from "**ANY** tax, income or otherwise" including of course, for that matter, surtax. We believe that a surtax is still a tax, albeit, an additional tax imposed in an amount already taxed. In effect, it is a Tax on a Tax. As it is still a tax, petitioners should be exempted therefrom as provided for by the aforesaid law.

Moreover, We again subscribe to the observation of the petitioners that "assuming, arguendo, that the 25%

tax on accumulated surplus was in fact a penalty, and not a tax, and that this 'penalty' was therefore not embraced within the tax exemption conferred by Section 4 (2)(b) of P.D. No. 1399 and Section 13 (2)(b) of P.D. No. 1869, then its repeal (by Section 6 Executive Order No. 37) should have retroactive effect and benefit the petitioners in accordance with the familiar principle that the repeal of penal provisions should be given retroactive effect insofar as they favor the persons affected thereby" (Phrase insertion and emphasis supplied; CTA Records, p. 257)

WHEREFORE, in all the foregoing, the assessments issued against the petitioners for alleged deficiency income tax, business tax and surtax from 1981 to 1985 are hereby declared **CANCELLED.**

SO ORDERED.

RAMON O. DE VEYRA
Associate Judge

2??

WE CONCUR:

Concurring and
(Dissenting Opinion)
ERNESTO D. ACOSTA
Presiding Judge

MANUEL K. GRUBA
Associate Judge

CERTIFICATION

I hereby certify that this decision was reached after due consultation between the members of the Court of Tax Appeals in accordance with Section 13, Article VIII of the **Constitution.**

ERNESTO D. ACOSTA
Presiding Judge
Court of Tax Appeals

296

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CONCURRING AND DISSENTING OPINION

I concur with the findings that in general petitioners enjoy tax exemption privileges by reason of their contractual relationship to operate and to provide facilities for gambling with PAGCOR. Under Section 13(2)(b) of PD 1869 the tax exemption

297

privileges enjoyed by PAGCOR is extended to other corporation be reason of existing contractual relationship with PAGCOR "in connection with operation of casino" or as a "result of essential facilities furnished and/or technical services rendered to the corporation or operator". "Registration" and "affiliation" are not mentioned by the provision of law as precondition to the enjoyment of the tax exemption privilege.

However, one exception to the tax exemption privileges is the imposition of income tax on dividend received by private stockholders of PAGCOR (Section 13(3) of PD 1869). Inasmuch as the tax exemption privilege of PAGCOR is merely extended by operation of law to other corporation having contractual relationship with the former, it follows that the private stockholders of petitioners should likewise be subjected to income tax on dividends they will receive.

The actuation of petitioners of unjustly accumulating their surplus profits instead of declaring dividends prevented the government from imposing income tax on dividends against their stockholders. This gives rise to the right of the government to impose the 25% surtax under Section 25 of the 1977 Tax Code, partly quoted below:

> "SEC. 25. Additional tax on corporations improperly accumulating profits or surplus. - (a) Imposition of tax. - If any corporation, except banks, insurance companies or personal holding companies whether domestic or foreign, is formed or availed of for the purpose of preventing the imposition of the tax upon its shareholders or members of another corporation, through the medium of permitting its gains and profits to accumulate instead of being divided or distributed, there is levied and assessed against such corporation, for each taxable year, a tax equal to twenty-five per centum of the undistributed portion of its accumulated profits or surplus which shall be in addition to the tax imposed by Section twenty-four, and shall be computed, collected and paid in the same manner and subject to the same provisions of law, including penalties, as that tax."

To hold otherwise is to defeat the very purpose of Section 25 of the Tax Code and Section 13(3) of PD 1869 because if we will interpret the latter law as exempting petitioners from the surtax then we will be encouraging them from not declaring dividends thereby preventing the government from collecting income tax on dividends. The imposition of surtax on unjust accumulation of surplus profit and the non-imposition of tax on dividends go hand in hand.

299

So that when income on dividends was abolished under Executive Order No. 37 on July 31, 1986, the provision on surtax was likewise abolished. One does not serve any purpose without the other.

Secondly, I agree with the respondent that the additional 25% surtax is actually not a tax but a penalty as held in **United Equipment & supply co. vs. Commissioner of Internal Revenue** (C.T.A. Case No. 1795, October 30, 1971, appeal denied *en banc* in G.R. No. L-35653, October 25, 1972, cited in **Commissioner of Internal Revenue vs. Ayala Securities Corporation**, 101 SCRA 231) as follows:

> "Although petitioner filed an income tax return, no return was filed covering its surplus profits which were improperly accumulated. In fact, no return could have been filed, and the law could not possibly require, for obvious reasons, the filing of a return covering unreasonable accumulation of corporate surplus profits. A tax imposed upon unreasonable accumulation of surplus is in the nature of penalty. (Helvering vs. National Grocery Co., 304 U.S. 282). It would not be proper for the law to compel a corporation to report improper accumulation of surplus. Accordingly, Section 331 limiting the right to assess internal revenue taxes within five years from the date the return was filed or was due does not apply."

Following the rule that tax exemptions are strictly construed against the taxpayer claiming

300

the same, the exemption from tax herein claimed under PD 1869 could not possibly cover improper accumulation of profits or surplus since the surtax is actually not a tax but a penalty. It is not normally imposed unless a taxpayer violated Section 25 of the said old Tax Code.

In the instant case based on petitioners' audited financial statements, Philippine Casino has improperly accumulated its profits from 1981 to 1985 and Provident International from 1981 to 1986. The records do not show sufficient justification for such accumulation.

Accordingly, assessment on surtax against accumulation of surplus profit should stand.

Quezon City, Metro Manila.

Ernesto D. Acosta

ERNESTO D. ACOSTA
Presiding Judge

301