REPUBLIC OF THE PHILIPPINES
**COURT OF TAX APPEALS**
QUEZON CITY

*Third Division*

**THE ORCHARD GOLF AND COUNTRY CLUB, INC.,**
*Petitioner,*

-versus-

**COMMISSIONER OF INTERNAL REVENUE,**
*Respondent.*

**CTA Case No. 8986**

Members:
**UY,** ***Chairperson,***
**RINGPIS-LIBAN,** *and*
**MODESTO-SAN PEDRO,** ***JJ.***

Promulgated:

JAN 14 2020
3:50 p.m.

X-----------------------------------------------------------------------------------------X

# DECISION

**RINGPIS-LIBAN, *J.*:**

The present *Petition for Review* filed by The Orchard Golf and Country Club, Inc. prays for the cancellation of the Final Assessment Notice dated March 28, 2014, bearing an aggregate deficiency tax of ₱113,766,847.77 for taxable year 2010.[1]

## THE PARTIES

Petitioner The Orchard Golf and Country Club, Inc. is a domestic, non-profit corporation, organized and validly existing in accordance with the laws of the Republic of the Philippines, for the purpose of promoting the social, educational, and athletic activities among its stockholders, the main objective and undertaking of which will be the construction and maintenance of a golf

[1] Summary of the Case, Pre-Trial Order dated November 4, 2015, Docket – Vol. 3, p. 1474.

course, tennis courts, squash courts, swimming pools, and other indoor and outdoor related sports and recreational facilities, where no part of its income is distributable to its members/shareholders.[2]

On the other hand, Respondent is the Commissioner of the Bureau of Internal Revenue (BIR), with principal office address at the 5th Floor BIR National Office Building, Agham Road, Diliman, Quezon City.[3] Respondent, *motu proprio* or through his authorized representatives, has the power to assess deficiency taxes, and decide protests to disputed assessments, pursuant to Section 4, in relation to Section 228, both of the National Internal Revenue Code (NIRC), as amended.[4]

On September 19, 2012, Petitioner received the Letter of Authority (LOA) No. LOA-54A-2012-00000102 dated September 13, 2012,[5] authorizing Revenue Herbert Ordiz and Group Supervisor Romanito Guiuan, to examine Petitioner's books of accounts and other accounting records for the period January 1, 2010 to December 31, 2010.

On March 26, 2014, Petitioner received a Preliminary Assessment Notice (PAN) issued on February 17, 2014,[6] which states that Petitioner is liable for deficiency taxes for taxable year 2010 in the aggregate amount of ₱113,033,316.81.[7]

Subsequently, on April 10, 2014, Petitioner filed the *Request for Reinvestigation* dated April 8, 2014, in respect of the said PAN.[8]

On April 21, 2014, Petitioner received the Formal Letter of Demand (or Final Assessment Notice) (FLD/FAN) issued on March 28, 2014.[9] In the FLD/FAN, Petitioner was found liable for deficiency taxes in the aggregate amount of ₱113,766,847.77[10] for transactions in 2010,[11] detailed as follows:

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[2] Par. 1.1, Stipulation of Facts, *Joint Stipulation of Facts and Issues* (JSFI), Docket – Vol. 3, p. 1429.

[3] Par. 2, *Petition for Review*, vis-à-vis, Par.1, *Answer*, Docket – Vol. 1, pp. 7 and 632, respectively.

[4] Par. 2.1, *Petition for Review*, vis-à-vis, Par.1, *Answer*, Docket – Vol. 1, pp. 7 and 632, respectively.

[5] Exhibit "P-12", Docket – Vol. 8, p. 3721; Exhibit "R-1", BIR Records, Folder 1, p. 47.

[6] Pars. 1.2 and 1.3, Stipulation of Facts, JSFI, Docket – Vol. 3, p. 1429.

[7] Exhibit "P-2", Docket – Vol. 6, pp. 3017 to 3020; Exhibit "R-14", BIR Records, Folder 1, p. 169 to 172; Par. 1.10, Stipulation of Facts, JSFI, Docket – Vol. 3, p. 1430.

[8] Par. 1.4, Stipulation of Facts, JSFI, Docket – Vol. 3, p. 1430; Exhibit "P-4", Docket – Vol. 6, pp. 3028 to 3048; Exhibit "R-16", BIR Records, Folder 2, pp. 157 to 177.

[9] Pars. 1.5 and 1.6, Stipulation of Facts, JSFI, Docket – Vol. 3, p. 1430.

[10] Exhibit "P-3", Docket – Vol. 6, pp. 3021 to 3027; Exhibit "R-15", BIR Records, Folder 1, pp. 155 to 158; and Par. 10, *Petition for Review*, vis-à-vis, Par. 1, *Answer*, Docket – Vol. 1, pp. 10 and 632, respectively.

[11] Par. 1.7 and 1.10, Stipulation of Facts, JSFI, Docket – Vol. 3, p. 1430.

| **I. INCOME TAX** | Amount in PHP | Amount in PHP |
|---|---|---|
| Net Loss per ITR | | (4,705,782.00) |
| Add: NOLCO | 4,705,782.00 | |
| Adjustments – Annex A | 176,686,694.91 | 181,392,476.91 |
| Taxable Income per Investigation | | 176,686,694.91 |
| Tax Due | | 53,006,008.47 |
| Less: Creditable Withholding Tax | | - |
| Deficiency Income Tax | | 53,006,008.47 |
| Add: Interest (April 16, 2011 to March 20, 2014) | | 31,048,450.99 |
| **Total Amount Payable** | | **84,054,459.46** |
| **II. VALUE ADDED TAX** | | |
| Taxable Sales per BIR ITS | | 92,862,356.60 |
| Add: Adjustments – Annex A | | 118,366,706.40 |
| Taxable Income per Investigation | | 211,229,063.00 |
| Multiply by Rate | | 12% |
| Total Output Tax Due | | 25,347,487.56 |
| Less: Payments | 681,971.68 | |
| Input Tax | 10,931,589.03 | |
| Less: Creditable VAT to be carried over the next period | 194,764.43 | 11,418,796.28 |
| Deficiency Tax | | 13,928,691.28 |
| Add: 50% Surcharge | 6,964,345.64 | |
| Interest (January 26, 2011 to March 20, 2014) | 8,769,351.91 | 15,733,697.03 |
| **Total Amount Payable** | | **29,662,388.31** |
| **III. COMPROMISE PENALTY** | | |
| Late Payment of Income Tax | | 50,000.00 |
| **Total Amount Payable** | | 50,000.00 |
| **GRAND TOTAL** | | **113,766,847.77** |

Thus, on May 21, 2014, Petitioner filed the Request for Reinvestigation dated May 21, 2014, in respect of the said FLD/FAN.[12]

On July 21, 2014, the Petitioner submitted documents to support its Request for Reinvestigation.[13]

On February 16, 2015, Petitioner filed the instant Petition for Review.[14]

[12] Par. 1.8, Stipulation of Facts, JSFI, Docket – Vol. 3, p. 1430; Exhibit "P-5", Docket – Vol. 7, pp. 3206 to 3226.

[13] Par. 1.9, Stipulation of Facts, JSFI, Docket – Vol. 3, p. 1430; Exhibits "P-6" and "P-7", Docket – Vol. 7, pp. 3462 to 3470.

[14] Docket – Vol. 1, pp. 6 to 56.

Within the extended time granted by the Court,[15] Respondent filed his Answer on May 12, 2015,[16] interposing the following special and affirmative defenses, to wit:

"**SPECIAL AND AFFIRMATIVE DEFENSES**

**Petitioner is liable for income tax.**

4. Sec. 27 of the NIRC is explicit:

SEC. 27. Rates of Income Tax on Domestic Corporations. -

(A) In General. - Except as otherwise provided in this Code, an income tax of thirty-five percent (35%) is hereby imposed upon the taxable income derived during each taxable year from all sources within and without the Philippines by every corporation, as defined in Section 22(B) of this Code and taxable under this Title as a corporation, organized in, or existing under the laws of the Philippines: Provided, That effective January 1, 1998, the rate of income tax shall be thirty-four percent (34%); effective January 1, 1999, the rate shall be thirty-three percent (33%); and effective January 1, 2000 and thereafter, the rate shall be thirty-two percent (32%).

In the case of corporations adopting the fiscal-year accounting period, the taxable income shall be computed without regard to the specific date when specific sales, purchases and other transactions occur. Their income and expenses for the fiscal year shall be deemed to have been earned and spent equally for each month of the period.

The reduced corporate income tax rates shall be applied on the amount computed by multiplying the number of months covered by the new rates within the fiscal year by the taxable income of the corporation for the period, divided by twelve.

Provided, further, That the President, upon the recommendation of the Secretary of Finance, may, effective January 1, 2000, allow corporations the

[15] Resolutions dated April 8, 2015 and May 8, 2015, Docket – Vol. 1, pp. 623 and 630 to 631, respectively.

[16] Docket – Vol. 1, pp. 632 to 645.

option to be taxed at fifteen percent (15%) of gross income as defined herein, after the following conditions have been satisfied:

(1) A tax effort ratio of twenty percent (20%) of Gross National Product (GNP);
(2) A ratio of forty percent (40%) of income tax collection to total tax revenues;
(3) A VAT tax effort of four percent (4%) of GNP; and
(4) A 0.9 percent (0.9%) ratio of the Consolidated Public Sector Financial Position (CPSFP) to GNP.

The option to be taxed based on gross income shall be available only to firms whose ratio of cost of sales to gross sales or receipts from all sources does not exceed fifty-five percent (55%).

The election of the gross income tax option by the corporation shall be irrevocable for three (3) consecutive taxable years during which the corporation is qualified under the scheme.

For purposes of this Section, the term 'gross income' derived from business shall be equivalent to gross sales less sales returns, discounts and allowances and cost of goods sold. 'Cost of goods sold' shall include all business expenses directly incurred to produce the merchandise to bring them to their present location and use.

For a trading or merchandising concern, 'cost of goods sold' shall include the invoice cost of the goods sold, plus import duties, freight in transporting the goods to the place where the goods are actually sold, including insurance while the goods are in transit.

For a manufacturing concern, 'cost of goods manufactured and sold' shall include all costs of production of finished goods, such as raw materials used, direct labor and manufacturing overhead, freight cost, insurance premiums and other costs incurred to bring the raw materials to the factory or warehouse.

In the case of taxpayers engaged in the sale of service, 'gross income' means gross receipts less sales returns, allowances and discounts.

(B) Proprietary Educational Institutions and Hospitals. - Proprietary educational institutions and hospitals which are nonprofit shall pay a tax of ten percent (10%) on their taxable income except those covered by Subsection (D) hereof: Provided, That if the gross income from unrelated trade, business or other activity exceeds fifty percent (50%) of the total gross income derived by such educational institutions or hospitals from all sources, the tax prescribed in Subsection (A) hereof shall be imposed on the entire taxable income. For purposes of this Subsection, the term 'unrelated trade, business or other activity' means any trade, business or other activity, the conduct of which is not substantially related to the exercise or performance by such educational institution or hospital of its primary purpose or function. A "proprietary educational institution' is any private school maintained and administered by private individuals or groups with an issued permit to operate from the Department of Education, Culture and Sports (DECS), or the Commission on Higher Education (CHED), or the Technical Education and Skills Development Authority (TESDA), as the case may be, in accordance with existing laws and regulations.

(C) Government-owned or Controlled-Corporations, Agencies or Instrumentalities. - The provisions of existing special or general laws to the contrary notwithstanding, all corporations, agencies, or instrumentalities owned or controlled by the Government, except the Government Service Insurance System (GSIS), the Social Security System (SSS), the Philippine Health Insurance Corporation (PHIC), the Philippine Charity Sweepstakes Office (PCSO) and the Philippine Amusement and Gaming Corporation (PAGCOR), shall pay such rate of tax upon their taxable income as are imposed by this Section upon corporations or associations engaged in a similar business, industry, or activity.

(D) Rates of Tax on Certain Passive Incomes. -

(1) Interest from Deposits and Yield or any other Monetary Benefit from Deposit Substitutes and from Trust Funds and Similar Arrangements, and Royalties. - A final tax at the rate of twenty percent (20%) is hereby imposed upon the amount of

interest on currency bank deposit and yield or any other monetary benefit from deposit substitutes and from trust funds and similar arrangements received by domestic corporations, and royalties, derived from sources within the Philippines: Provided, however, That interest income derived by a domestic corporation from a depository bank under the expanded foreign currency deposit system shall be subject to a final income tax at the rate of seven and one-half percent (7 1/2%) of such interest income.

(2) Capital Gains from the Sale of Shares of Stock Not Traded in the Stock Exchange. - A final tax at the rates prescribed below shall be imposed on net capital gains realized during the taxable year from the sale, exchange or other disposition of shares of stock in a domestic corporation except shares sold or disposed of through the stock exchange:

Not over P100,000..........................5%
Amount in excess of P100,000.......10%

(3) Tax on Income Derived under the Expanded Foreign Currency Deposit System. - Income derived by a depository bank under the expanded foreign currency deposit system from foreign currency transactions with local commercial banks, including branches of foreign banks that may be authorized by the Bangko Sentral ng Pilipinas (BSP) to transact business with foreign currency depository system units and other depository banks under the expanded foreign currency deposit system, including interest income from foreign currency loans granted by such depository banks under said expanded foreign currency deposit system to residents, shall be subject to a final income tax at the rate of ten percent (10%) of such income.

Any income of nonresidents, whether individuals or corporations, from transactions with depository banks under the expanded system shall be exempt from income tax.

(4) Intercorporate Dividends. - Dividends received by a domestic corporation from another domestic corporation shall not be subject to tax.

(5) Capital Gains Realized from the Sale, Exchange or Disposition of Lands and/or Buildings. - A final

tax of six percent (6%) is hereby imposed on the gain presumed to have been realized on the sale, exchange or disposition of lands and/or buildings which are not actually used in the business of a corporation and are treated as capital assets, based on the gross selling price or fair market value as determined in accordance with Section 6(E) of this Code, whichever is higher, of such lands and/or buildings.

(E) Minimum Corporate Income Tax on Domestic Corporations. -

(1) Imposition of Tax. - A minimum corporate income tax of two percent (2%) of gross income as of the end of the taxable year, as defined herein, is hereby imposed on a corporation taxable under this Title, beginning on the fourth taxable year immediately following the year in which such corporation commenced its business operations, when the minimum income tax is greater than the tax computed under Subsection (A) of this Section for the taxable year.

(2) Carry Forward of Excess Minimum Tax. - Any excess of the minimum corporate income tax over the normal income tax as computed under Subsection (A) of this Section shall be carried forward and credited against the normal income tax for the three (3) immediately succeeding taxable years.

(3) Relief from the Minimum Corporate Income Tax Under Certain Conditions. - The Secretary of Finance is hereby authorized to suspend the imposition of the minimum corporate income tax on any corporation which suffers losses on account of prolonged labor dispute, or because of force majeure, or because of legitimate business reverses.

The Secretary of Finance is hereby authorized to promulgate, upon recommendation of the Commissioner, the necessary rules and regulations that shall define the terms and conditions under which he may suspend the imposition of the minimum corporate income tax in a meritorious case.

> (4) Gross Income Defined. - For purposes of applying the minimum corporate income tax provided under Subsection (E) hereof, the term 'gross income' shall mean gross sales less sales returns, discounts and allowances and cost of goods sold. 'Cost of goods sold' shall include all business expenses directly incurred to produce the merchandise to bring them to their present location and use.
>
> For a trading or merchandising concern, 'cost of goods sold' shall include the invoice cost of the goods sold, plus import duties, freight in transporting the goods to the place where the goods are actually sold including insurance while the goods are in transit.
>
> For a manufacturing concern, 'cost of goods manufactured and sold' shall include all costs of production of finished goods, such as raw materials used, direct labor and manufacturing overhead, freight cost, insurance premiums and other costs incurred to bring the raw materials to the factory or warehouse.
>
> In the case of taxpayers engaged in the sale of service, 'gross income' means gross receipts less sales returns, allowances, discounts and cost of services. 'Cost of services' shall mean all direct costs and expenses necessarily incurred to provide the services required by the customers and clients including (A) salaries and employee benefits of personnel, consultants and specialists directly rendering the service and (B) cost of facilities directly utilized in providing the service such as depreciation or rental of equipment used and cost of supplies

5. RMC 25-2012 promulgated on 3 August 2012, specifically states that clubs organized and operated exclusively for pleasure, recreation and other non-profit purposes shall now be subject to income tax and VAT.

6. It must be stressed that the tax exemption given to clubs had not been carried over in the 1997 NIRC. The exemption on having been deleted in the revision of the NIRC, the lawmaker's intention to remove the exemption granted to recreational clubs is clear.

7. RMC 25-2012 merely clarifies and restates Section 27 of the NIRC with regard to income tax of corporations which states that corporations are subject to income tax.

8. Previously, in the NIRC code of 1977, clubs organized and operated exclusively for pleasure, recreation, and other non-profit purposes were exempt from income tax.

9. However, this exemption was not found in the new NIRC of 1997.

10. Following to the doctrine of *casus omissus pro omisso habendus est*, a person, object or thing omitted from an enumeration must be held to have been omitted intentionally. Hence, the income of recreational clubs from whatever source, including but not limited to membership fees assessment dues, rental income, and service fees are subject to income tax.

11. Also, Petitioner argues that under Sec, 30(E) of the NIRC, it is still exempt from income tax. However, tax exemptions are never presumed and are strictly construed against a taxpayer.

12. Worthy to note, Sec. 30 of the NIRC states that:

xxx

> Notwithstanding the provisions in the preceding paragraphs, the income of whatever kind and character of the foregoing organizations from any of their properties, real or personal, or from any of their activities conducted for profit regardless of the disposition made of such income, shall be subject to tax imposed under this Code.

13. It is clear from the above cited provision that Petitioner does not qualify under the tax exemption. Petitioner cannot simply claim by its own base assertion that as a non-stock institution, it is automatically exempt from payment of taxes.

14. The Honorable Supreme Court in the case of *Diaz and Timbol vs. Secretary of Finance and the Commissioner of Internal Revenue* made it explicit:

> Tax exemptions must be justified by clear statutory grant and based on language in the law too plain to be mistaken. xxx The Court is thus duty-bound to simply apply the law as it is found.

> Lastly, the grant of tax exemption is a matter of legislative policy that is within the exclusive prerogative of Congress. The Courts role is to merely uphold this legislative policy, as reflected first and foremost in the language of the tax statute. Thus, any unwarranted burden that may be perceived to result from enforcing such policy must be properly referred to Congress. The Court has no discretion on the matter but simply applies the law.

15. The assailed RMC was explicit that clubs which are organized and operated exclusively for pleasure, recreation and other non-profit purposes are subject to income tax under the Tax Code of 1997 as amended. Taxation is the rule and exemption is the exception.

16. Regarding Petitioner's argument that RMC 35-2012 should not be applied retroactively, again Petitioner's argument does not hold water. Petitioner is being taxed for income tax under Sec. 27 of the NIRC. RMC 35-2012 only calls for the strict implementation of Sec. 27 of the NIRC, similar to the case of *Philam vs. Sec. of Finance and CIR*:

> Lastly, Petitioner is mistaken in stating that RMC 25-11, having been issued after the sale, was being applied retroactively in contravention to Sec. 246 of the NIRC. **Instead, it merely called for the strict application of Sec. 100, which was already in force the moment the NIRC was enacted. (emphasis supplied**)

**Petitioner is liable to pay VAT**

17. By simply stating that the amount paid cannot be subjected to VAT because it is in the form of a subsidy to defray its expenses would open the doors to each person claiming VAT-exemption, as indeed every person or entity would treat its income as a 'subsidy' to defray its expenses.

18. Contrary to Petitioner's statement when a member pays the dues/fees, there is an actual sale of service. The service that the club offers to the members are the exclusive and preferential right to enjoy the facilities of the clubs, as well as other privileges enjoyed by its members.

19. Petitioner is liable for VAT as imposed under Sec. 105 in relation to Sec. 108 of the NIRC, as amended, thus:

SEC. 105. Persons Liable. - Any person who, in the course of trade or business, sells barters, exchanges, leases goods or properties, renders services, and any person who imports goods shall be subject to the value-added tax (VAT) imposed in Sections 106 to 108 of this Code.

The value-added tax is an indirect tax and the amount of tax may be shifted or passed on to the buyer, transferee or lessee of the goods, properties or services. This rule shall likewise apply to existing contracts of sale or lease of goods, properties or services at the time of the effectivity of Republic Act No. 7716.

The phrase 'in the course of trade or business' means the regular conduct or pursuit of a commercial or an economic activity, including transactions incidental thereto, by any person regardless of whether or not the person engaged therein is a nonstock, nonprofit private organization (irrespective of the disposition of its net income and whether or not it sells exclusively to members or their guests), or government entity.

The rule of regularity, to the contrary notwithstanding, services as defined in this Code rendered in the Philippines by nonresident foreign persons shall be considered as being course of trade or business.

SEC. 108. Value-added Tax on Sale of Services and Use or Lease of Properties.

(A) Rate and Base of Tax. - There shall be levied, assessed and collected, a value-added tax equivalent to ten percent (10%) of gross receipts derived from the sale or exchange of services, including the use or lease of properties.

The phrase 'sale or exchange of services' means the performance of all kinds or services in the Philippines for others for a fee, remuneration or consideration, including those performed or rendered by construction and service contractors; stock, real estate, commercial, customs and immigration brokers; lessors of property, whether personal or real; warehousing services; lessors or distributors of cinematographic films; persons engaged in milling processing, manufacturing or repacking goods for others; proprietors, operators or keepers of hotels, motels, resthouses, pension houses, inns, resorts; proprietors or operators of restaurants, refreshment parlors, cafes and other eating places, including clubs and caterers; dealers in securities; lending investors; transportation contractors on their transport of goods or cargoes, including persons who transport goods or cargoes for hire another domestic common carriers by land, air and water relative to their transport of goods or cargoes; services of franchise grantees of telephone and telegraph, radio and television broadcasting and all other franchise grantees except those under Section 119 of this Code; services of banks, non-bank financial intermediaries and finance companies; and non-life insurance companies (except their crop insurances), including surety, fidelity, indemnity and bonding companies; and similar services regardless of whether or not the performance thereof calls for the exercise or use of the physical or mental faculties. The phrase 'sale or exchange of services' shall likewise include:

(1) The lease or the use of or the right or privilege to use any copyright, patent, design or model, plan secret formula or process, goodwill, trademark, trade brand or other like property or right;

(2) The lease of the use of, or the right to use of any industrial, commercial or scientific equipment;

(3) The supply of scientific, technical, industrial or commercial knowledge or information;

(4) The supply of any assistance that is ancillary and subsidiary to and is furnished as a means of enabling the application or enjoyment of any such property, or right as is mentioned in subparagraph (2) or any such knowledge or information as is mentioned in subparagraph (3);

(5) The supply of services by a nonresident person or his employee in connection with the use of property or rights belonging to, or the installation or operation of any brand, machinery or other apparatus purchased from such nonresident person.

> (6) The supply of technical advice, assistance or services rendered in connection with technical management or administration of any scientific, industrial or commercial undertaking, venture, project or scheme;
>
> (7) The lease of motion picture films, films, tapes and discs; and
>
> (8) The lease or the use of or the right to use radio, television, satellite transmission and cable television time.
>
> Lease of properties shall be subject to the tax herein imposed irrespective of the place where the contract of lease or licensing agreement was executed if the property is leased or used in the Philippines.
>
> The term 'gross receipts' means the total amount of money or its equivalent representing the contract price, compensation, service fee, rental or royalty, including the amount charged for materials supplied with the services and deposits and advanced payments actually or constructively received during the taxable quarter for the services performed or to be performed for another person, excluding value-added tax.

20. As stated above, the phrase 'in the course of trade or business' means the regular conduct or pursuit of a commercial or an economic activity, including transactions incidental thereto, by any person regardless of whether or not the person engaged therein is a nonstock, nonprofit private organization (irrespective of the disposition of its net income and whether or not it sells exclusively to members or their guests), or government entity.

21. It is also clear from the above stated provision that even a non-stock, non-profit organization or entity would be liable to pay VAT. This conclusion was already affirmed by the Supreme Court in the case of *Commissioner of Internal Revenue vs. Court of Appeals and Commonwealth Management and Services Corporation*, viz:

> Contrary to COMASERCO's contention the above provision clarifies that even a non-stock, non-profit, organization or government entity, is liable to pay VAT on the sale of goods or services. **VAT is a tax**

**on transactions, imposed at every stage of the distribution process on the sale, barter, exchange of goods or property, and on the performance of services, even in the absence of profit attributable thereto. The term 'in the course of trade or business' requires the regular conduct or pursuit of a commercial or an economic activity regardless of whether or not the entity is profit-oriented.**

The definition of the term 'in the course of trade or business' present law applies to all transactions even to those made prior to its enactment. Executive Order No. 273 stated that any person who, in the course of trade or business, sells, barters or exchanges goods and services, was already liable to pay VAT. The present law merely stresses that even a nonstock, nonprofit organization or government entity is liable to pay VAT for the sale of goods and services.

Sec. 108 of the National Internal Revenue Code of 1997 10 defines the phrase 'sale of services' as the 'performance of all kinds of services for others for a fee, remuneration or consideration.' It includes 'the supply of technical advice, assistance or services rendered in connection with technical management or administration of any scientific, industrial or commercial undertaking or project.'

xxx

Hence, it is immaterial whether the primary purpose of a corporation indicates that it receives payments for services rendered to its affiliates on a reimbursement-on-cost basis only, without realizing profit, for purposes of determining liability for VAT on services rendered. As long as the entity provides service for a fee, remuneration or consideration, then the service rendered is subject to VAT.

At any rate, it is a rule that because taxes are the lifeblood of the nation, statutes that allow exemptions are construed strictly against the grantee and liberally in favor of the government. Otherwise stated, any exemption from the payment of a tax must be clearly stated in the language of the law; it cannot be merely implied therefrom. **In the case of VAT, Section 109, Republic Act 8424 clearly**

**enumerates the transactions exempted from VAT. The services rendered by COMASERCO do not fall within the exemptions.**

22. Sec. 109 of the NIRC enumerates the transactions which are VAT-exempt, applying the principle of *expressio unius est exclusio alterius*, it is clear that Congress deemed that income of recreational clubs, membership dues included, are subject to VAT.

23. And again, to further stress that these recreational clubs are subject to VAT, the doctrine of *casus omissus pro omisso habendus est* should also be bore in mind *(sic)* that Congress intentionally omitted said recreational clubs from being Income tax and VAT-exempt.

24. Petitioner is also contesting certain entries in the FAN such as the disallowed salaries and wages, and other expenses. However, well-settled is the rule that tax assessments are entitled to the presumption of correctness and made in good faith. The taxpayer has the duty to prove otherwise. In the absence of proof of any irregularities in the performance of duties, an assessment duly made by a Bureau of Internal Revenue examiner and approved by his superior officers will not be disturbed. All presumptions are in favor of the correctness of tax assessments.

25. The burden of proof is on the taxpayer contesting the validity or correctness of an assessment to prove not only that the Commissioner of Internal Revenue is wrong but the taxpayer is right. Otherwise the presumption of correctness of tax assessment stands. The presumption in favor of the correctness of tax assessment stands where evidence to the contrary is wanting. Hence, the assessment issued against Petitioner is imbued with factual and legal bases."

The Pre-Trial Conference was initially set on June 30, 2015.[17] However, upon the filing of an Urgent Motion To Defer Pre-Trial Conference by Respondent on June 23, 2015,[18] the Pre-Trial Conference was reset to, and was held on, September 1, 2015.[19]

Petitioner filed its Pre-Trial Brief on June 25, 2015;[20] while the Pre-Trial for the Respondent was filed on August 27, 2015.[21]

[17] Notice of Pre-Trial Conference dated May 14, 2015, Docket – Vol. 1, pp. 647 to 648.

[18] Docket – Vol. 1, pp. 649 to 652.

[19] Minutes of the hearing held on June 30, 2015, Docket – Vol. 1, p. 720; Minutes of the hearing held on September 1, 2015, Docket – Vol. 3, p. 1404.

[20] Docket – Vol. 2, pp. 720 to 732.

[21] Docket – Vol. 3, pp. 1383 to 1387.

The parties filed their Joint Stipulation of Facts and Issues on September 11, 2015.[22] This was adopted by the Court in the Pre-Trial Order dated November 4, 2015,[23] which also deemed the Pre-Trial Conference terminated.

The trial of the case proceeded.

During trial, Petitioner presented documentary and testimonial evidence. The following are Petitioner's witnesses: (1) Mr. Denis Hilarion B. Nuevo,[24] Senior Manager for Administration of Petitioner; (2) Ms. Ma. Fedna B. Parallag,[25] the Court-commissioned Independent Certified Public Accountant (ICPA);[26] and (3) Mr. Jose Ernilo Famy,[27] its Financial Comptroller and Senior Manager for Purchasing and Management Information System.

On March 31, 2016, the Petitioner's Formal Offer Ad Cautelam was filed.[28] In the Resolution dated April 16, 2018,[29] the Court admitted most of Petitioner's exhibits, *except* the following:

1) Exhibits "P-15-124", "P-16-1,439", "P-16-1,440", "P-16-1,863" to "P-16-1882", "P-16-2,261", "P-16-2,267", "P-16-2,268", "P-16-2,411", "P-16-3,937", "P-16-5,738", "P-16-6,149", "P-16-8,227", "P-16-8,228", "P-16-8,846" to "P-16-8,856", "P-16-9,153", "P-16-9,578", "P-16-9,641", "P-16-9,642", "P-16-9,714", "P-16-9,723", "P-16-10,121", "P-16-10,339", "P-16-10,589", "P-16-13,030", "P-16-13,406", "P-16-13,567" to "P-16-13,569", "P-16-14,055", "P-17-6-13", "P-17-6-24", "P-24-121" to "P-24-123", and "P-24-332", for not being found the records; and

2) Exhibits "P-17-6-25" to "P-17-6-26", for failure to identify.

On June 24, 2016, the Petitioner's Supplemental Formal Offer of Evidence was filed.[30] In the Resolution dated July 14, 2016,[31] the Court resolved the said Supplemental Formal Offer of Evidence, and admitted Exhibits "P-40", "P-41", "P-42 to P-42-DK", "P-43 and P-43-1".

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[22] Docket – Vol. 3, pp. 1429 to 1437.

[23] Docket – Vol. 3, pp. 1474 to 1482.

[24] Exhibit "P-34", Docket – Vol. 2, pp. 1029 to 1034; Minutes of the hearings held on November 9, 2015 and January 19, 2016, Docket – Vol. 3, pp. 1483 and 1708.

[25] Exhibit "P-36", Docket – Vol. 3, pp. 1609 to 1655; Minutes of the hearing held on January 19, 2016, Docket – Vol. 3, p. 1708.

[26] Minutes of the hearing held on, and *Oath of Commission* dated, September 28, 2015, Docket – Vol. 3, pp. 1439 to 1440.

[27] Exhibit "P-39", Docket – Vol. 4, pp. 1772 to 1805; Exhibit "P-43", Docket – Vol. 8, pp. 3817 to 3821; Minutes of the hearings held on March 8, 2016 and June 14, 2016, Docket – Vols. 6 and 8, pp. 2916 and 3852, respectively.

[28] Docket – Vol. 6, pp. 2934 to 2971.

[29] Docket – Vol. 8, pp. 4055 to 4057.

[30] Docket – Vol. 8, pp. 3857 to 3859.

[31] Docket – Vol. 8, pp. 3932 to 3933,

Respondent likewise presented his documentary and testimonial evidence. His witnesses were Revenue Officers Herbert Ordiz,[32] Edwin Artumba,[33] and Geoffrey H. Rivarez.[34] He filed his *Formal Offer of Evidence* on February 17, 2017.[35]

On March 9, 2017, Petitioner filed a Motion to Expunge Respondent's Written Formal Offer of Evidence.[36] However, the said Motion to Expunge was denied by the Court in the Resolution dated May 2, 2017.[37]

In the Resolution dated July 6, 2017,[38] the Court admitted Exhibits "R-1", "R-2", "R-3", "R-4", "R-5", "R-6", "R-7", "R-8", "R-9", "R-10", "R-11", "R-12", "R-13", "R-14", "R-15", "R-16", "R-17", "R-18", "R-19", "R-20", "R-21", "R-22" and "R-22-1"; but denied the admission of Exhibit "R-15-A", for not having been found in the records of the case.

Respondent filed his Memorandum on November 26, 2018.[39]

On December 13, 2018, Petitioner filed a Motion to Admit Memorandum (With attached Memorandum dated 13 December 2018).[40] The said Motion to Admit was granted by the Court in the Resolution dated January 23, 2019,[41] thereby admitting Petitioner's Memorandum,[42] and submitting the instant case for decision.

## THE ISSUES

The parties raised the following issues[43] for resolution of this Court, *viz*:

**"Main Issue:**

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[32] Exhibit "R-20", Docket – Vol. 3, pp. 1378 to 1382; Minutes of the hearing held on, and Order dated, August 1, 2016, Docket – Vol. 8, pp. 3934 to 3935.

[33] Exhibit "R-21", Docket – Vol. 3, pp. 1397 to 1400; Minutes of the hearing held on, and Order dated, November 7, 2016, Docket – Vol. 8, pp. 3938 to 3939.

[34] Exhibit "R-22", Docket – Vol. 3, pp. 1410 to 1414; Minutes of the hearing held on, and Order dated, February 6, 2017, Docket – Vol. 8, pp. 3940 to 3942.

[35] Docket – Vol. 8, pp. 3944 to 3950.

[36] Docket – Vol. 8, pp. 3953 to 3955.

[37] Docket – Vol. 8, pp. 3965 to 3967.

[38] Docket – Vol. 8, pp. 3978 to 3979.

[39] Docket – Vol. 8, pp. 4098 to 4113.

[40] Docket – Vol. 9, pp. 4189 to 4191.

[41] Docket – Vol. 9, pp. 4253 to 4254.

[42] Docket – Vol. 9, pp. 4192 to 4248.

[43] Issues, JSFI, Docket – Vol. 3, pp. 1430 to 1431.

Whether or not Formal Letter of Demand (or Final Assessment Notice) dated 28 March 2014 is valid, and the Petitioner is liable for deficiency taxes, interests, surcharges and/or penalties in the aggregate amount of Pesos: One Hundred Thirteen Million Seven Hundred Sixty-Six Thousand Eight Hundred Forty-Seven and 77/100 (PHP113,766,847.77).

**Sub-Issues:**

2.1 Whether or not the membership dues paid to the Petitioner are subject to income taxes;

2.2 Whether or not the membership dues paid to the Petitioner are subject to value added taxes;

2.3 Whether or not RMC No. 35-2012 may be given retroactive application".

## THE ARGUMENTS OF THE PARTIES

Petitioner argues that the FAN is null and void because Respondent violated Section 228 of the NIRC of 1997, Revenue Regulation (RR) No. 12-99, and the PAN itself, thereby denying Petitioner its constitutional right to due process.

Moreover, Petitioner contends that the reinvestigation granted to it was a sham because the officer who allegedly conducted the reinvestigation did not even know the facts and arguments of the case, and thus, the reinvestigation was merely for show, to give the appearance that Petitioner was afforded the change to be heard.

Petitioner also claims that the amount ₱129,509,513.00 deemed under the FAN as "undeclared sales" is not income, but represents the capital contributions of the members of Petitioner in the form of membership fees or monthly association dues. It contends that the monthly dues paid by the Petitioner's members are akin to condominium dues, which are held merely in trust to be used solely for administrative expenses, and the maintenance of Petitioner's facilities.

Furthermore, according to Petitioner, Respondent's construction of the tax-exempt corporations under Section 30 of the NIRC of 1997, as embodied in Revenue Memorandum Circular (RMC) No. 35-2012, proceeds from a misapplication of the doctrine *casus omissus pro omisso habendus est.*

In addition, Petitioner avers that RMC No. 13-2012 cannot be given retroactive effect because it will prejudice Petitioner and other similarly situated corporations and organizations.

Petitioner also points out that the ICPA has concluded that Respondent's disallowance of its salaries and wages expense amounting to ₱27,385,834.35 due to alleged unsubstantiated expenses is erroneous, and that such expenses are fully substantiated; that Respondent's disallowance of expenses pertaining to Member Relations, Tournament Expenses, Provisions for Impairment of Assets, and Provisions for Contingencies, is erroneous, and all such expenses have been substantiated; that the expenses (collection fees) in the amount of ₱1,628,029.60 incurred by Petitioner were paid through credit card, and since the credit card company is the constituted withholding agent, these should not be subjected withholding; and that the disallowed Professional Fees amounting to ₱2,186,949.00 pertain to *honoraria* or *per diems* of the members of its board of directors for their attendance at board meetings, which Petitioner properly subjected to withholding tax.

It is further contended by Petitioner that it is not liable for deficiency VAT; and that since Petitioner has a 2010 Net Operating Loss Carry-Over (NOLCO) which remains unutilized in the amount of ₱126,616,132.00, Petitioner is not liable for any income tax deficiency.

Lastly, Petitioner contends that the imposition of surcharges and penalties under the FAN have no factual or legal basis.

On the other hand, Respondent claims that Petitioner is liable for income tax; that RMC No. 25-2012 promulgated on August 2, 2012, specifically states that clubs organized and operated exclusively for pleasure, recreation and other non-profit purposes shall now be subject to income tax and VAT; that RMC No. 25-2012 merely clarifies and restates Section 27 of the NIRC of 1997, with regard to income tax of corporations.

Moreover, Respondent contends that previously, clubs organized and operated exclusively for pleasure, recreation, and other non-profit purposes were exempt from income tax. However, this exemption was not found in the NIRC of 1997, as amended. Thus, following the doctrine *casus omissus pro omisso habendus est*, a person, object or thing omitted from an enumeration must be held to have been omitted intentionally, the income of recreational clubs from whatever source, including but not limited to membership fees assessment dues, rental income, and service fees are subject to income tax.

Respondent also argues that Petitioner is liable to pay value-added tax (VAT). He contends that contrary to Petitioner's statement, when a member pays the dues/fees, there is an actual sale of service; and that the service that

Petitioner offers to its members are the exclusive and preferential right to enjoy the facilities of Petitioner, as well as other privileges enjoyed by its members.

## THE RULING OF THE COURT

The instant Petition for Review is meritorious.

Petitioner argues that the FAN is null and void because Petitioner violated Section 228 of the NIRC of 1997, RR No. 12-99, and the PAN itself, thereby denying Petitioner its constitutional right to due process.

We agree with Petitioner.

Section 228 of the NIRC of 1997 provides as follows:

> "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 taxpayers shall be informed in writing of the law and the facts on which the assessment is made; otherwise, the assessment shall be void.
>
> **Within a period to be prescribed by implementing rules and regulations, the taxpayer shall be required to respond to said notice. If the taxpayer fails to respond, the Commissioner or his duly authorized representative shall issue an assessment based on his findings.**
>
> 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.
>
> If the protest is denied in whole or in part, or is not acted upon within one hundred eighty (180) days from submission of documents, the taxpayer adversely affected by the decision or inaction may appeal to the Court of Tax Appeals within thirty (30) days from receipt of the said decision, or from the lapse of the

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one hundred eighty (180)-day period; otherwise, the decision shall become final, executory and demandable." *(Emphases supplied)*

To implement the foregoing provision, Section 3 of RR No. 12-99,[44] as amended by RR No. 18-2013,[45] provides, in part, as follows:

"SECTION 3. *Due Process Requirement in the Issuance of a Deficiency Tax Assessment.* —

3.1 Mode of procedures in the issuance of a deficiency tax assessment:

xxx xxx xxx

3.1.1 *Preliminary Assessment Notice* (PAN). – **If after review and evaluation by the Commissioner or his duly authorized representative, as the case may be, it is determined that there exists sufficient basis to assess the taxpayer for any deficiency tax or taxes, the said Office <u>shall issue to the taxpayer a Preliminary Assessment Notice (PAN) for the proposed assessment</u>.** It shall show in detail the facts and the law, rules and regulations, or jurisprudence on which the proposed assessment is based xxx.

**If the taxpayer fails to respond within fifteen (15) days from date of receipt of the PAN, he shall be considered in default, <u>in which case, a Formal Letter of Demand and Final Assessment Notice (FLD/FAN) shall be issued</u> calling for payment of the taxpayer's deficiency tax liability, inclusive of the applicable penalties.**

If the taxpayer, within fifteen (15) days from date of receipt of the PAN, responds that he/it disagrees with the finding of deficiency tax or taxes, an FLD/FAN shall be issued within fifteen (15) days from filing/submission of the taxpayer's response, calling for payment of the taxpayer's deficiency tax liability, inclusive of the applicable penalties.

xxx xxx xxx

3.1.3 *Formal Letter of Demand and Final Assessment Notice (FLD/FAN).* - The Formal Letter of Demand and Final

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[44] SUBJECT: Implementing the Provisions of the National Internal Revenue Code of 1997 Governing the Rules on Assessment of National Internal Revenue Taxes, Civil Penalties and Interest and the Extra-Judicial Settlement of a Taxpayer's Criminal Violation of the Code Through Payment of a Suggested Compromise Penalty.

[45] SUBJECT: Amending Certain Sections of Revenue Regulations No. 12-99 Relative to the Due Process Requirement in the Issuance of a Deficiency Tax Assessment, November 28, 2013.

> Assessment Notice (FLD/FAN) shall be issued by the Commissioner or his duly authorized representative. The FLD /FAN calling for payments 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 assessment shall be void.
>
> xxx xxx xxx" (*Emphases and underscoring ours*)

Based on the foregoing provisions, as part of due process in the issuance of tax assessments, a taxpayer is given fifteen (15) days from receipt of the PAN to file a protest or response thereto with the BIR. It is only upon the lapse of the prescribed 15-day period, without such protest or response being filed by the taxpayer within such period, that Respondent may issue the corresponding FLD or FAN.

Relative thereto, in *Commissioner of Internal Revenue vs. Avon Products Manufacturing, Inc., etseq.*,[46] the Supreme Court said:

> "**Tax assessments issued in violation of the due process rights of a taxpayer are null and void.** While the government has an interest in the swift collection of taxes, the Bureau of Internal Revenue and is officers and agents cannot be overreaching in their efforts, but must perform their duties in accordance with law, with their own rules of procedure, and always with regard to the basic tenets of due process.
>
> The 1997 National Internal Revenue Code, also known as the Tax Code, and revenue regulations allow a taxpayer to file a reply or otherwise submit comments or arguments with supporting documents at each stage in the assessment process. **Due process requires the Bureau of Internal Revenue to consider defenses and evidence submitted by the taxpayer and to render a decision based on these submissions. Failure to adhere to these requirements constitutes a denial of due process and taints the administrative proceedings with invalidity.**
>
> xxx xxx xxx
>
> The Bureau of Internal Revenue is the primary agency tasked to assess and collect proper taxes, and to administer and enforce the Tax Code. To perform its functions of tax assessment and collection properly, it is given ample powers under the Tax Code, such as the power to examine tax returns

[46] G.R. Nos. 201398-99, and 201418-19, October 3, 2018.

> and books of accounts, to issue a subpoena, and to assess based on the best evidence obtainable, among others. **However, these powers must 'be exercised reasonably and [under] the prescribed procedure.' The Commissioner and revenue officers must strictly comply with the requirements of the law, with the Bureau of Internal Revenue's own rules, and with due regard to taxpayer's constitutional rights.**
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> xxx xxx xxx
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> xxx. **Tax investigation and assessment necessarily demand the observance of due process because they affect the proprietary rights of specific persons.**
>
> xxx xxx xxx
>
> **Administrative due process is anchored on fairness and equity in procedure.** xxx, it demands that the party's defenses be considered by the administrative body in making its conclusions, and that the party be sufficiently informed of the reasons for its conclusions.
>
> xxx xxx xxx
>
> xxx. **The right to be heard,** which includes the right to present evidence, **is meaningless if the Commissioner can simply ignore the evidence without reason.**
>
> xxx xxx xxx
>
> **While indeed the government has an interest in the swift collection of taxes, its assessment and collection should be exercised justly and fairly, and always in strict adherence to the requirements of the law and of the Bureau of Internal Revenue's own rules.**" *(Emphases and underscoring ours)*

Based on the foregoing doctrinal pronouncements, Respondent or the BIR is mandated to perform its assessment functions in accordance with law, and strict adherence thereto, with their own rules of procedure, and always with regard to the basic tenets of due process. Moreover, part of the administrative due process requirement is the recognition by the BIR that the taxpayer has the right to present evidence, and thus, should be allowed to submit comments or arguments with supporting documents ***at each stage*** in the assessment process. And in case Respondent or the BIR fails to observe due process, it shall have the effect of rendering the deficiency tax assessment void, and of no force and effect.

In this case, the PAN dated February 17, 2014[47] was received by Petitioner only on March 26, 2014.[48] By virtue of the aforequoted Section 3 of RR No. 12-99, as amended by RR No. 18-2013, Petitioner had fifteen (15) days or until April 10, 2014, within which to protest or respond to the said PAN.

However, Respondent issued the subject FLD/FAN on March 28, 2014,[49] or barely two (2) days from Petitioner's receipt of the PAN, and before the lapse of the said 15-day period for it to protest or respond thereto. Thus, the FLD/FAN was clearly issued prematurely thereby depriving Respondent of the opportunity to be heard on the PAN, in violation of the due process requirement in the issuance of tax assessments.

While it may be true that Petitioner was able to file its Request for Reinvestigation dated April 8, 2014, with respect to the PAN, on April 10, 2014,[50] the premature issuance of the subject FLD/FAN on March 28, 2014 has divested Petitioner of its right to submit its comments or arguments with supporting documents at one stage in the assessment process. This clearly constitutes denial of due process as Petitioner was not given the opportunity to dispute and present evidence against the PAN, before the final assessment was issued.

Correspondingly, since the subject deficiency tax assessments were issued in violation of Petitioner's due process rights, the same are null and void. As such, the said deficiency tax assessments bear no valid fruit,[51] and must not be given any effect.

In view of the nullity of the subject tax assessments, this Court finds it unnecessary to address the remaining issues raised in the instant case.

**WHEREFORE**, in light of the foregoing considerations, the instant Petition for Review is **GRANTED**. Accordingly, the FLD/FAN dated March 28, 2014, assessing Petitioner for deficiency taxes in the aggregate amount of ₱113,766,847.77, for taxable year 2010, is **CANCELLED** and **SET ASIDE**.

**SO ORDERED.**

**MA. BELEN M. RINGPIS-LIBAN**
*Associate Justice*

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[47] Exhibit "P-2", Docket – Vol. 6, pp. 3017 to 3020; Exhibit "R-14", BIR Records, Folder 1, p. 169 to 172.

[48] Pars. 1.2 and 1.3, Stipulation of Facts, JSFI, Docket – Vol. 3, p. 1429.

[49] Par. 1.5, Stipulation of Facts, JSFI, Docket – Vol. 3, p. 1430.

[50] Par. 1.4, Stipulation of Facts, JSFI, Docket – Vol. 3, p. 1430; Exhibit "P-4", Docket – Vol. 6, pp. 3028 to 3048; Exhibit "R-16", BIR Records, Folder 2, pp. 157 to 177.

[51] *Commissioner of Internal Revenue vs. Liquigaz Philippines Corporation, etseq.*, G.R. Nos. 215534 and 215557, April 18, 2016.

**WE CONCUR:**

**ERLINDA P. UY**
Associate Justice

**MARIA ROWENA MODESTO- SAN PEDRO**
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.

**ERLINDA P. UY**
*Associate Justice*
*Chairperson*

## CERTIFICATION

Pursuant to Section 13 of Article VIII 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's Division.

**ROMAN G. DEL ROSARIO**
*Presiding Justice*