REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

ATENEO DE MANILA UNIVERSITY,
Petitioner,

- versus - C.T.A. CASE NO. 4280

THE COMMISSIONER OF INTERNAL REVENUE,
Respondent.

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7/12/93

D E C I S I O N

Before this Court is a question of whether or not a non-stock, non-profit educational institution, engaged in undertaking research sponsored by various government agencies, private international non-profit organizations, and other entities, is an independent contractor subject to contractor's tax pursuant to the provision of Sec. 205 of the National Internal Revenue Code of 1977, as amended by Presidential Decree No. 69.

Briefly, the undisputed facts as gathered from the records and the evidence adduced by the parties are as follows:

The petitioner, Ateneo de Manila University, is a non-stock, non-profit educational institution with auxiliary units and branches all over the nation. One such auxiliary unit is the Institute of Philippine Culture (IPC for brevity) which has no legal personality separate and distinct from that of the petitioner. The IPC is a research unit engaged in social science studies of Philippine society and culture. For this purpose, the IPC conducts research which it hopes will contribute to the advancement of knowledge, especially of Philippine society and culture that will eventually lead to an improvement in the quality of life of the Filipinos. With such noble objectives, the aspirations of IPC are shared by other international organizations, private foundations, and government agencies which are willing to sponsor research in similar undertakings (Memorandum for the Petitioner, C.T.A. Records, p. 190).

On July 8, 1983, petitioner received from the respondent Commissioner of Internal Revenue a demand letter, dated June 3, 1983, assessing petitioner the sum of P174,043.97

for deficiency contractor's tax, and an assessment, dated June 27, 1983, in the sum of P1,141,837.76 for deficiency income tax, both for the fiscal year ended March 31, 1978.

On August 1, 1983, petitioner protested the above assessments through a letter, dated July 28, 1983. An eleven-page memorandum, dated October 3, 1983, was thereafter filed with the respondent on October 4, 1983 contesting the validity of the assessments, together with the required waiver of the defense of prescription.

Respondent, in a letter-decision of March 17, 1988 which was received by the petitioner on May 16, 1988, cancelled the assessment for deficiency income tax and modified the assessment for deficiency contractor's tax by increasing the amount due to P193,475.55.

On June 14, 1988, petitioner requested for a reconsideration or reinvestigation of the modified assessment. On the same date, petitioner filed this petition for review.

While the case was pending before this Court, respondent, in reply to petitioner's request, issued a final decision dated August 3, 1988 modifying the assessment for deficiency contractor's tax from P193,475.55 to P46,516.41 exclusive of surcharge and interest computed as follows:

IPC revenue on sponsored research for the fiscal year ended March 31, 1978	P1,550,547.00
Contractor's tax rate	3 %
Deficiency contractor's tax	P 46,516.41

Respondent, in support of his assessment, stated in his letter-decision addressed to the petitioner's counsel that:

> "For rendering research work to various government agencies and international non-profit organizations as part of its educational thrust, the University is considered an independent contractor pursuant to the provision of then Section 205 of the Tax Code; hence, its gross receipts in the amount of P1,550,547.00 is subject to the 3% contractor's tax. The fact that no profit is realized by your client from its activities of rendering sponsored research does not relieve it from paying the 3% contractor's tax because the contractor's tax being an excise tax imposed on the exercise of a privilege, is collectible from the person exercising the privilege. Hence, your client should pay the 3% contractor's tax on the basis of the total gross receipts derived from the sponsored research which amounted to P1,550,547.00 during the fiscal year under review."

Section 205 of the 1977 Tax Code, as amended, reads:

> "Sec. 205. *Contractors, proprietors or operators of dockyards, and others.* - A contractor's tax of three *per centum* of the gross receipts is hereby imposed on the following:
>
> xxx xxx xxx
>
> (16) Business agents and other independent contractors except persons, associations and corporations under contract for embroidery and apparel for export, as well as their agents and contractors and except gross receipts of or from a pioneer industry registered with the Board of Investments under the provisions of Republic Act No. 5186;
>
> xxx xxx xxx
>
> The term "independent contractors" include persons (juridical or natural) not enumerated above (but not including individuals subject to the occupation tax under Section 12 of the local Tax Code) whose activity consists <u>essentially of the sale of all kinds of services for a fee</u> regardless of whether or not the performance of the service calls for the exercise or use of the physical or mental faculties of such contractors or their employees. (Underscoring supplied)
>
> xxx xxx xxx."

In the case of Luzon Stevedoring Co. vs. Trinidad[1] (43 Phil 803) the Supreme Court defined the word "contractor" as

> "xxx a person who, in the <u>pursuit of an independent business</u>, undertakes to do a specific piece or job of work for other persons, *using his own means and methods without submitting himself to control as to the petty details.* The true test of a

[1]See also Commissioner of Internal Revenue v. Court of Tax Appeals, 143 SCRA 49; Commissioner of Internal Revenue v. Engineering Equipment and Supply Company, 64 SCRA 590; La Carlota Sugar Central v. Trinidad, 43 Phil. 816.

> 'contractor' would seem to be that he renders the service in the course of an independent occupation, representing the will of his employer only as to the result of his work, and not as to the means by which it is accomplished." (Underscoring supplied)

Is petitioner an independent contractor within the purview of the provision of the Tax Code and the jurisprudence above-cited?

Respondent tried to impress this Court that the term "independent contractor" encompasses all kinds of services rendered for a fee and that the only exceptions are the following:

a. Persons, associations and corporations under contract for embroidery and apparel for export;

b. Gross receipts of or from pioneer industry registered with the Board of Investment under R.A. No. 5186;

c. Individuals subject to occupation tax under Sec. 12 of the Local Tax Code; and

d. Regional or area headquarters established in the Philippines by multinational corporations, including their alien executives, and which headquarters do not earn or derive income from the Philippines and which act as supervisory, communication and coordinating centers for their affiliates, subsidiaries or branches in the Asia Pacific Region.

Respondent concluded that since petitioner falls under the definition of an independent contractor and is not among the exceptions, it is therefore subject to the 3% contractor's tax (Memorandum for Respondent, C.T.A. Records, pp. 213-214).

This Court rules otherwise.

It is true that exceptions, deductions and amnesty are matters of legislative grace and should be construed in *strictissimi juris* against the taxpayer and liberally in favor of the taxing authority (Philippine Petroleum Corporation v. Municipality of Pililla, Rizal, 198 SCRA 82), but statutes levying taxes or duties are to be construed strongly against the Government and in favor of the subjects or citizens, because burdens are not imposed or presumed to be imposed beyond what statutes expressly and clearly declare. (Commissioner of Internal Revenue v. Court of Appeals, 204 SCRA 182).

In the case at bar, this Court, with the latter presumption in mind, should first determine if petitioner is covered by the term "independent contractor" as defined in Sec. 205 of the Tax Code. If it is, then the respondent is correct in relying on the first presumption; otherwise, there is no room for such interpretation. In plain words, the general provision of a tax law is liberally construed in favor of the taxpayer whereas its exception is strictly construed against him.

The tax provision in question states that "persons xxx whose activity consists essentially of the sale of all kinds of service for a fee xxx" are liable for contractor's tax. It is clear therefore that for one to be made liable, he must be engaged in business. Contractor's tax is a business tax under Title V of the Tax Code.

Business is restricted to activities or affairs where profit is the purpose or livelihood is the motive. (Commissioner of Internal Revenue v. Club Filipino, Inc., 5 SCRA 321; Collector of Internal Revenue v. Manila Lodge, 105 Phil 983) Business is that which occupies the time, attention and labor of men for the purpose of livelihood or profit (Bouvier's Law Dictionary, Third Revision, 1975 Ed.).

Petitioner maybe considered a "contractor" or an "independent contractor in a generic sense of the word(s) but is definitely not a "contractor" or an "independent contractor" as contemplated in Sec. 205 of the Tax Code. The latter has but a limited and restricted meaning; that is, one whose activity consists essentially of the sale of all kinds of services for a fee, or one who pursues an independent business, or one who renders service in the course of an independent occupation.

As correctly argued by the petitioner, it is not liable for contractor's tax since:

1. Research is a mandated activity for petitioner to retain its university status; and

2. Petitioner is not engaged in business as it has no profit motive, it retains ownership of results of the research and the right to publish such results, and it does not undertake proprietary nor commercial research (Memorandum for Petitioner, C.T.A. Records, pp. 194-206).

In the case of U.S.T. Press vs. National Labor Union (6 SCRA 317), the Supreme Court, while maintaining that U.S.T. Press is neither a natural or judicial person and has no personality to be a party in a case in its own right ruled:

> "It may be true that the U.S.T. Press used to accept outside printing jobs, but this work is merely incidental, for its main function is to do jobs coming from the University of Santo Tomas and its departments or from the Dominican Fathers. Moreover, the record is not clear that in so accepting outside printing jobs the press realized profits. And even assuming that it made profits from such work, the fact still remains that there is no proof that part of such earnings or profits was ever distributed as dividends to any stockholder, as in fact none was so distributed because they accrued to the benefit of the University of Santo Tomas which is a non-profit educational institution."

Petitioner was able to show that IPC had incurred losses from 1972 to 1985. Respondent however alleged that since contractor's tax is an excise tax imposed on the exercise of a privilege, having losses or no realized profit does not relieve petitioner from paying the tax. This Court considers the accumulated losses as proof that education and not profit is the motive for undertaking the research projects. The respondent's allegation is therefore totally misplaced.

The Supreme Court in the cases of Club Filipino, Inc. and Manila Lodge (supra) held:

"Having found as a fact that the Club was organized to develop and cultivate sports of all class and denomination, for the healthful recreation and entertainment of its stockholders and members; that upon its dissolution, its remaining assets, after paying debts, shall be donated to a charitable Philippine Institution in Cebu; that it is operated mainly with funds derived from membership fees and dues; that the Club's bar and restaurant catered only to its members and their guests; that there was in fact no cash dividend distribution to its stockholders and that whatever was derived on retail from its bar and restaurant was used to defray its overall overhead expenses and to improve its golf-course (cost-plus-expenses-basis), it stands to reason that the Club is not engaged in the business of an operator of bar and restaurant xxx."

"xxx. The privilege taxes prescribed in section 193 of the Tax Code in relation to section 178 of the same, are to be imposed only on persons or entities who engage in the activities mentioned or classified therein for 'business' purposes. This evident intention of the law becomes more palpable when we take into consideration the fact that the drafters of our Tax Code had grouped the aforequoted provisions of law under one general division of the Tax Code headed as 'Title V, Privilege Taxes on *Business and occupation*.'

It is not therefore entirely correct to maintain as respondent does, that all persons selling articles subject to specific taxes, like liquor and tobacco, should likewise be subject to the fixed taxes imposed by section 193 of the Tax Code. We believe, that in order that these persons should be subjected to the privilege taxes imposed by the aforementioned section of the Tax Code, it is necessary that they be engaged in the 'business' of selling liquor and tobacco, otherwise the privilege taxes as a dealer of liquor and tobacco can not attach."

The funds received by the petitioner are technically not a fee. They may however fall as gifts or donations which are tax-exempt. IPC, for the fiscal year ended March 31, 1978, had the following revenues, costs and expenses: (Exhibit "F", CTA Records, p. 125)

	Sponsored Research	Publication	Total
Revenues	P1,550,547.00	P63,854.00	P1,614,401.00
Direct Costs	1,329,761.00	53,775.00	1,383,536.00
Gross Profit	P 220,786.00	P10,079.00	P 230,865.00
Other Income			P 110,995.00
Gross Income			P 341,860.00
Indirect Expenses			397,049.00
Net Loss			P 55,189.00

In compliance with Sec. 123 of the Tax Code*, less than thirty *per centum* (P220,786.00/P1,550,547.00 = 14.24%) of the

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*Sec. 123. *Exemption of certain gifts.* - The following gifts or donations shall be exempt from the tax provided for in this Chapter:

a) In the case of gifts made by a resident:

xxx xxx xxx

3) Gifts in favor of an educational and or charitable, religious, cultural or social welfare corporation, institution, foundation, trust or philanthropic organization or research institution or organization: *Provided, however,* That not more than thirty *per centum* of said gifts shall be used by such donee for administration purposes.

For the purpose of this exemption, a non-profit educational and/or charitable corporation, institution, foundation, trust or philanthropic organization and/or research institution or organization is a school, college or university and/or charitable corporation, foundation, trust or philanthropic organization and/or research institution, or organization, incorporated as a non-stock entity, paying no dividends, governed by trustees who receive no compensation, devoting all its income, whether student's fees, or gifts, donations, subsidies or other forms or philanthropy, to the accomplishment and promotion of the purposes enumerated in its articles of incorporation.

xxx xxx xxx.

gross revenue was made available for administration purposes.

WHEREFORE, in view of the foregoing, respondent's decision is SET ASIDE. The deficiency contractor's tax assessment in the amount of P46,516.41 exclusive of surcharge and interest for the fiscal year ended March 31, 1978 is hereby CANCELLED. No pronouncement as to cost.

SO ORDERED.

Quezon City, Metro Manila, July 12, 1993.

RAMON O. DE VEYRA
Associate Judge

WE CONCUR:

ERNESTO D. ACOSTA
Presiding Judge

MANUEL K. GRUBA
Associate Judge

CERTIFICATION

I hereby certify that this decision was reached after due consultation among 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