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TAX LAW FOR BUSINESS

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Stringent rules in availing tax exemption

IT has always been said that tax exemptions must be construed strictly against the taxpayer and liberally in favor of the taxing authority. However, if the law expressly exempts a particular entity, business, industry or transaction from tax, then the tax exemption should be respected accordingly.

Section 30 of the Tax Code expressly enumerates the organizations and associations exempt from paying income tax on income received by them as such. In 2013, however, the Bureau of Internal Revenue (BIR) issued Revenue Memorandum Order (RMO) 020-13 stating that the BIR accords tax-exempt status to these corporations and associations by way of confirmatory BIR rulings or certificates of tax exemption, which are issued after due evaluation of documents submitted by said corporations and associations. Based on said memorandum order, it is the BIR which accords the tax-exemption status to these tax-exempt corporations through the issuance of rulings or exemption certificates. Accordingly, the memorandum order requires these corporations and associations to file applications for tax exemptions with the appropriate BIR office.

Oppositions to this issuance were raised by various sectors. In fact, there were judicial decisions issued against the said order. In the case of The Abbas'orchard School Inc. v. CIR, CTA Case No. 8377, November 4, 2014, the court ruled that when the Tax Code does not provide for a requirement to be exempt, the BIR cannot add an additional requirement to implement the law.

Thus, a nonstock, nonprofit educational institution should only prove that no part of its income is derived from activities conducted for profit.

Further, the requirement for certificate of exemption prescribed in RMO 020-13 is not a requirement stated by the Tax Code. Therefore, the certificate of exemption is not a condition precedent for the exempt entity to be entitled to its exemption.

In its effort to clarify RMO 020- 13, the BIR issued RMO 34-14. The said RMO acknowledged that tax-exemption rulings do not confer tax-exemptions, which are not provided for by law, nor can tax-exemption rulings abrogate those exemptions, which are granted by law. The absence of a valid tax-exemption ruling will not operate to divest qualified entities of the tax exemption provided under the Constitution or the Tax Code. These entities that fail to secure a tax-exemption ruling are duty bound to prove compliance with the conditions laid down by the law and other pertinent administrative issuances in the event of a tax investigation. In essence, a ruling is not required, provided that if an issue is raised during examination relative to tax exemption, the entity is bound to prove its entitlement.

However, the BIR reiterated its earlier issuance that the failure of the nonstock, nonprofit entity to present its valid, current and subsisting tax-exemption ruling to its appropriate withholding agents, shall subject such entity to the payment of the withholding taxes due on their transactions.

On the other hand, the withholding agent's failure to withhold notwithstanding, the lack of tax-exemption ruling shall cause the imposition of penalties. Since the withholding agents bear the burden of penalties for failure to withhold in the absence of a tax-exemption ruling presented by the payee, these payors are forced to require, and the payees are forced to present tax-exemption rulings. Otherwise, the payor has to withhold tax on the payment. In effect, the supposed tax-exempt organization is still required to secure tax-exemption ruling so that its receipts are not subjected to withholding taxes.

There are always ways to tax transactions that are supposedly exempt from tax. In a recent ruling (BIR Ruling No. 26-16) supposedly secured in compliance with the above memorandum orders, the BIR ruled that once an association is value-added tax registered, the taxpayer is automatically presumed to be engaged in business. Hence, such entity will not qualify for exemption under Section 30 of the Tax Code. It is still liable for income tax and value-added tax or percentage tax.

A lesson from this ruling is that taxpayers should, aside from complying with the requirement for securing tax-exemption ruling, be careful with the types of taxes that they register as applicable to them. These types of registered taxes may affect their exemption from income taxes.

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