



September 30, 2013

**HON. KIM S. JACINTO-HENARES**

Commissioner of Internal Revenue

**BUREAU OF INTERNAL REVENUE**

4/F, BIR National Office Building

BIR Road, Diliman

Quezon City

Subject: Revenue Memorandum Order No. 20-2013

Dear Honorable Commissioner Henares:

We, the Catholic Educational Association of the Philippines ("CEAP"), a corporation duly organized and existing under the laws of the Philippines as a non-stock, non-profit ("NSNP") religious corporation, write on behalf of our Catholic educational institution member-schools ("Member-Schools") in connection with the issuance of Revenue Memorandum Order ("RMO") No. 20-2013.

We understand that RMO No. 20-2013 was issued in order to enhance the monitoring of certain corporations and associations enumerated under Section 30, National Internal Revenue Code of 1997<sup>1</sup> ("Tax Code") which are exempt from paying income tax on income received by them as such. However, a closer scrutiny of the provisions of RMO No. 20-2013 reveals that the non-filing or denial of the Application for Tax Exemption/Revalidation made by these corporations and associations have the effect of disqualifying these corporations and associations from availing of their tax-exempt status as provided in the Tax Code. Essentially, RMO No. 20-2013 results in disqualifying corporations and associations from availing the tax exemption in the event of non-compliance with the policies and guidelines stated therein and, thus deprive these institutions of such exemptions which are duly and expressly granted to them by law.

In light of the foregoing, we respectfully request the exemption of NSNP religious and educational institutions from the implementation of RMO No. 20-2013 based on the following grounds:

1. The 1987 Philippine Constitution (the "Constitution") and the Tax Code explicitly grant tax exemption to NSNP religious and educational institutions;

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<sup>1</sup> Republic Act No. 8424, as amended.



2. The issuance of RMO No. 20-2013 violates the Member-Schools' right to due process since –
  - a. The RMO imposes an additional, unreasonable, and unnecessary burden upon NSNP religious and educational institutions other than what is expressly stated in the law; and
  - b. The RMO was issued without due notice to the Member-Schools and public hearing on the matter covered by the RMO.

#### A. BACKGROUND

##### *CEAP and its Member-Schools*

CEAP was founded as an association of various Catholic educational institutions in the Philippines, with the aim of representing the interest of these educational institutions in national and international fora, fostering unity of action with other organizations in educational matters, and assisting members, particularly those in mission areas, to achieve common and specific aims. The primary purpose of CEAP is to advance and promote the educational work of the Catholic Church in the Philippines and contribute to the development of responsible citizenship among the young of the land.<sup>2</sup> Thus, CEAP is a NSNP religious institution.

Moreover, CEAP's 1,252 Member-Schools are, by themselves, NSNP educational institutions organized actually, directly, and exclusively for educational purposes. A sample list of CEAP's Member-Schools is attached to this letter as **Annex "A."**

##### *RMO No. 20-2013*

On July 22, 2013, the Bureau of Internal Revenue ("BIR") issued RMO No. 20-2013 requiring NSNP institutions to file an Application for Tax Exemption/Revalidation, along with the required supporting documents, with their respective Revenue District Office ("RDO") in order to maintain their tax-exempt status. Accordingly, under Section 8(a), RMO No. 20-2013, if an Application for Tax Exemption/Revalidation is not made or is denied, the NSNP institution may be held liable for deficiency taxes, penalties and interest beginning January 1, 2014.

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<sup>2</sup> Articles of Incorporation of CEAP, as amended (1941).



**B. DISCUSSION**

**1. CEAP and its Member-Schools are exempt from taxation under the law.**

Under Section 28(3), Article VI, Constitution, charitable institutions, churches and parsonages or convents appurtenant thereto, mosques, nonprofit cemeteries, and all lands, buildings, and improvements, actually, directly, and exclusively used for religious, charitable, or educational purposes shall be exempt from taxation. Moreover, under Section 4(3), Article XIV, Constitution, NSNP educational institutions are exempt from taxes and duties, to wit:

[A]ll revenues and assets of non-stock, non-profit educational institutions used actually, directly, and exclusively for educational purposes shall be exempt from taxes and duties. Moreover, proprietary educational institutions, including those cooperatively owned, may likewise be entitled to such exemptions subject to the limitations provided by law including restrictions on dividends and provisions for reinvestment.

These provisions in the Constitution were adopted and implemented in Section 30(E), Tax Code, which provides as follows:

*SEC. 30. Exemption from Tax on Corporations.* – The following organizations shall not be taxed under this Title in respect to income received by them as such:

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(E) Nonstock corporation or association organized and operated exclusively for religious, charitable, scientific, athletic, or cultural purposes, or for the rehabilitation of veterans, no part of its net income or asset shall belong to or inure to the benefit of any member, organizer, officer or any specific person;

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(H) A nonstock and nonprofit educational institution;

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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.<sup>3</sup>

Thus, under the Constitution and the Tax Code, NSNP religious and educational institutions are categorically granted tax exemption with respect to the income received by them as such. However, their income from properties or from any of their activities conducted for profit shall be subject to tax.

The rationale behind the Constitutional and Tax Code provisions on tax exemptions for NSNP educational institutions was explained during the deliberations of the 1986 Constitutional Commission thus:

The fundamental constitutional policy on education is that it is the duty of the State to make quality education available while at the same time affordable to as large a segment of the population as possible. Further, it is fundamental democratic policy that students should be able to go to schools of their choice, whether public or private.

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The constitutional provision thus has a threefold rationale. It is intended (1) to preserve the democratic choice of the students; (2) to enable educational institutions to improve their quality; and (3) to make quality education affordable.<sup>4</sup>

Thus, it is clear that the Constitution, and the Tax Code provision which implemented the policy therein, intended to protect the self-sustainability of educational institutions in the country by exempting them from income tax.

Nevertheless, the Supreme Court provided two (2) evidentiary requirements which an educational institution must prove in order to apply the tax exemption under the law. In the landmark case of Commissioner of Internal Revenue vs. Court of Appeals<sup>5</sup> (the “YMCA” case) the Court stated thus:

As previously discussed, laws allowing tax exemption are construed *strictissimi juris*. Hence, for the YMCA to be granted the exemption it claims under the aforesaid provision, it must prove with substantial evidence that (1) it falls under the classification non-stock, non-profit educational institution; and (2) the

<sup>3</sup> Underscoring supplied.

<sup>4</sup> Fr. Joaquin G. Bernas, S.J., THE 1987 CONSTITUTION OF THE REPUBLIC OF THE PHILIPPINES 1285-6 (2009 ed.).

<sup>5</sup> G.R. No. 124043, October 14, 1998.



income it seeks to be exempted from taxation is used actually, directly, and exclusively for educational purposes.<sup>6</sup>

In the foregoing case, the Court ruled that since the Young Men's Christian Association of the Philippines, Inc. ("YMCA") failed to prove that: (1) it was an educational institution and (2) the proportionate amount of the subject income that was actually, directly, and exclusively used for educational purposes, YMCA was subject to regular income tax on its rental income from the lease of its properties.

The same two-fold evidentiary test was applied by the Court of Tax Appeals ("CTA") in the recent case of Ateneo de Manila University vs. Commissioner of Internal Revenue<sup>7</sup> (the "Ateneo" case) which resolved the issue of whether concession fees paid by the cafeteria operators in the school premises constituted income which was exempt from tax pursuant to the Constitutional provision.

In Ateneo, the Court found that the educational institution, Ateneo de Manila University ("ADMU"), was able to comply with the two tests mentioned above and, therefore, was exempt from tax on its income from concession fees. Since both parties already stipulated on the fact that ADMU was a NSNP educational institution, the Court was left with an examination of whether the income sought to be exempted was used actually, directly, and exclusively for educational purposes. In this case, ADMU presented various financial statements and schedules which showed that even if the income from the concession fees was intermingled with other income in a general fund, the Summaries of Contribution and Expenditure for the covered years showed that the expenses and disbursements from the general fund was used for scholarship grants, faculty development, salary expenses of school employees, and the like. Thus, ADMU was able to prove that all of its income was used actually, directly, and exclusively for educational purposes in order to exempt it from income tax.

For the part of CEAP and its Member-Schools, we would like to point out that a determination of the foregoing requirements was already made by the BIR in its Ruling No. 159-98 dated November 11, 1998<sup>8</sup> wherein it was confirmed that all the revenues and assets of CEAP's Member-Schools, which are NSNP educational institutions, being used actually, directly and exclusively for educational purposes are exempt from taxes. Thus, the BIR succinctly ruled as follows:

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Thus, since all revenues and assets of the said educational institutions are being used actually, directly and exclusively for educational purposes are exempt from

<sup>6</sup> Underscoring supplied.

<sup>7</sup> CTA Cases No. 7246 and 7293, March 11, 2010.

<sup>8</sup> A copy of BIR Ruling No. 159-98 dated November 11, 1998 is attached hereto as **Annex "B"**.



taxes, which include internal revenue taxes under the National Internal Revenue Code, your opinion that said institutions are exempt from the aforementioned BIR-registration requirements is hereby confirmed.<sup>9</sup>

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Accordingly, the BIR ruled that CEAP's Member-Schools are exempt from the following:

1. keeping books of accounts registered with the BIR under Section 232, Tax Code;
2. registration of business name under Section 237, Tax Code; and
3. issuance of receipts and sales invoices printed with the permission of, and stamped by, the BIR, under Section 238, Tax Code.

As stated by the BIR in the ruling:

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In reply, please be informed that under Section 232 of the Tax Code of 1997 (also Section 232 of the Tax Code, as amended), only corporations, companies, partnerships or persons required by law to pay internal revenue taxes, are mandated to maintain and keep BIR-registered books of accounts. Likewise, under Section 236 of the Tax Code of 1997, only persons subject to any internal revenue taxes are required to register with the BIR their business names. Furthermore, Sections 237 and 238 both of the same Code, provide that only persons engaged in business and subject to an internal revenue tax are required to issue BIR-registered sales invoices and receipts.

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Nevertheless, and in accordance with the applicable jurisprudence, the BIR stated in BIR Ruling No. 159-98 that the exemption only applies to the educational activities of CEAP's Member-Schools. Thus, if the Member-Schools engaged in any business activity or transaction on which its Constitutional tax exemption is not applicable, such as lease of real property for commercial use, the aforementioned BIR registration requirements will have to be complied with. This notwithstanding, we should point out that CEAP's Member-Schools have likewise secured their own BIR Rulings confirming their tax exemption.

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<sup>9</sup> Underscoring supplied.



Therefore, CEAP and its Member-Schools are clearly and unequivocally exempt from tax pursuant to the Constitution and Section 30, Tax Code, as acknowledged and confirmed by the BIR in BIR Ruling No. 159-98.

2. *RMO No. 20-2013 invalidly restricts the tax exemption granted to NSNP religious and educational institutions.*

While RMO No. 20-2013 purports to “prescribe policies and guidelines in the issuance of tax exemption applications and revalidation of tax exemption rulings/certificates”<sup>10</sup>, it also mentions that the BIR “accords tax-exempt status” to those tax-exempt corporations and associations listed under Section 30, Tax Code by way of its issuance of confirmatory BIR Rulings or certificates of tax exemption. Accordingly, without the requisite BIR confirmation, a NSNP religious or educational institution cannot claim tax exemption.

We respectfully submit that RMO No. 20-2013, as mere administrative issuance which “prescribes the policies and guidelines in the issuance of tax exemption rulings to qualified non-stock, non-profit corporations and associations under Section 30 of the National Internal Revenue Code of 1997, as amended”, cannot defeat the provisions in the Constitution and/or the Tax Code. Hence, it cannot impose a condition precedent to the availment of the tax-exempt status clearly and unequivocally granted under both the Constitution and the Tax Code to NSNP religious and educational institutions.

As already stated above, we are aware that there is a requirement to the tax exemption as stated in the Constitution itself and confirmed by jurisprudence, particularly, that the NSNP religious or educational institutions prove that the income sought to be exempted from taxation is used actually, directly, and exclusively for educational purposes.<sup>11</sup> Nevertheless, it is submitted that this requirement was never contemplated by law to be a preliminary qualification for the NSNP religious or educational institutions to avail of the tax exemption granted by law. Rather, the tax exemption was already self-executory by its nature. Accordingly, the proof required of actual, direct, and exclusive use of income was only resorted to in cases of subsequent inquiry or investigation into these NSNP institutions.

Based on the foregoing, it is our position that RMO No. 20-2013 imposes an additional, unreasonable, and unnecessary burden upon the NSNP religious and educational institutions other than what is expressly stated in the law. As such, in requiring NSNP religious and educational institutions to secure tax exemption rulings/certificates, submit voluminous documents and comply with a laborious validation process, the BIR is invalidly restricting the

<sup>10</sup> Section 1, RMO No. 20-2013.

<sup>11</sup> Commissioner of Internal Revenue vs. Court of Appeals, G.R. No. 124043, October 14, 1998; and Ateneo de Manila University vs. Commissioner of Internal Revenue, CTA Case No. 7246, March 11, 2010.



tax exemptions granted to NSNP religious and educational institutions pursuant to the Constitution and the Tax Code. We believe that RMO No. 20-2013 has invalidly amended such Constitutional and Tax Code provisions by transforming what should have been a mere factual examination of NSNP religious and educational institutions into an administrative approval process backed up with the threat of disqualification from their present tax-exempt status.

3. *The RMO was issued without observing the Member-Schools' right to due notice and hearing*

The effect of RMO No. 20-2013 would be unreasonable since it interferes with the private business of operating an educational institution and imposes unnecessary restrictions upon a substantive Constitutional right without giving NSNP educational institutions the right to be heard. Accordingly, pursuant to settled jurisprudence, the BIR's issuance of the regulation would be considered a violation of the due process clause of the Constitution since it imposed, effectively, a new tax burden while failing to accord such taxpayers their right to due notice and hearing.

In the case of Commissioner of Internal Revenue vs. Court of Appeals, Court of Tax Appeals, and Fortune Tobacco Corporation<sup>12</sup>, the Supreme Court ruled that:

It should be understandable that when an administrative rule is merely interpretative in nature, its applicability needs nothing further than its bare issuance for it gives no real consequence more than what the law itself has already prescribed. When, upon the other hand, the administrative rule goes beyond merely providing for the means that can facilitate or render least cumbersome the implementation of the law but substantially adds to or increases the burden of those governed, it behooves the agency to accord at least to those directly affected a chance to be heard, and thereafter to be duly informed, before that new issuance is given the force and effect of law.<sup>13</sup>

Thus, in a recent case, the Supreme Court reiterated that public participation of affected taxpayers is necessary in cases where a government agency imposes a new tax burden:

Considering that the questioned regulation would affect the substantive rights of respondent as explained above, it therefore follows that petitioners should have applied the pertinent provisions of Book VII, Chapter 2 of the Revised Administrative Code, to wit:

<sup>12</sup> G.R. No. 119761, August 29, 1996.

<sup>13</sup> Underscoring supplied.





Section 3. *Filing.* -

- (1) Every agency shall file with the University of the Philippines Law Center three (3) certified copies of every rule adopted by it. Rules in force on the date of effectivity of this Code which are not filed within three (3) months from that date shall not thereafter be the bases of any sanction against any party of persons.

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Section 9. *Public Participation.* -

- (1) If not otherwise required by law, an agency shall, as far as practicable, publish or circulate notices of proposed rules and afford interested parties the opportunity to submit their views prior to the adoption of any rule.
- (2) In the fixing of rates, no rule or final order shall be valid unless the proposed rates shall have been published in a newspaper of general circulation at least two (2) weeks before the first hearing thereon.
- (3) In case of opposition, the rules on contested cases shall be observed.

Likewise, in *Tañada v. Tuvera*, we held:

The clear object of the above-quoted provision is to give the general public adequate notice of the various laws which are to regulate their actions and conduct as citizens. Without such notice and publication, there would be no basis for the application of the maxim "*ignorantia legis non excusat.*" It would be the height of injustice to punish or otherwise burden a citizen for the transgression of a law of which he had no notice whatsoever, not even a constructive one.

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Because petitioners failed to follow the requirements enumerated by the Revised Administrative Code, the assailed regulation must be struck down.<sup>14</sup>

<sup>14</sup> Commissioner of Customs and the District Collector of the Port of Subic vs. Hypermix Feeds Corporation, G.R. No. 179579, February 1, 2012.



Lastly, it should be noted that even as early as 1956, the Supreme Court already ruled that there should be no additional requirement, other than those contemplated in the law, for the application of a tax exemption.<sup>15</sup> Thus, in the case of Commissioner of Internal Revenue vs. Central Luzon Drug Corporation<sup>16</sup>, the Supreme Court saw it fit to remind the BIR that:

[T]he law cannot be amended by a mere regulation. In fact, a regulation that “operates to create a rule out of harmony with the statute is a mere nullity”; it cannot prevail.

[While i]t is a cardinal rule that courts “will and should respect the contemporaneous construction placed upon a statute by the executive officers whose duty it is to enforce it” . . . [c]ourts, however, will not uphold these authorities' interpretations when clearly absurd, erroneous or improper.

The administrative agency issuing these regulations may not enlarge, alter or restrict the provisions of the law it administers; it cannot engraft additional requirements not contemplated by the legislature.

In case of conflict, the law must prevail. A “regulation adopted pursuant to law is law.” Conversely, a regulation or any portion thereof not adopted pursuant to law is no law and has neither the force nor the effect of law.<sup>17</sup>

The basic tenets of due process and fair play demand that NSNP educational institutions, being such essential components of nation-building and social development that they were given tax exemptions by Constitutional policy, should be allowed to retain their tax-exempt status without need for subsequent administrative approval.

Moreover, it should be pointed out that since the BIR may still conduct regular post-audits of NSNP educational institutions in order to check for compliance with the jurisprudential rules enunciated in YMCA and Ateneo cases even without applying RMO No. 20-2013, the foregoing Application for Tax Exemption/Revalidation processes are already superfluous and unnecessary to begin with.

In this regard, we respectfully submit that RMO No. 20-2013 invalidly restricts the tax exemption granted to NSNP religious and educational institutions and should be declared as having been invalidly issued.

<sup>15</sup> Commissioner of Internal Revenue vs. V.G. Sinco Educational Institution, G.R. No. L-9276, October 23, 1956.

<sup>16</sup> G.R. No. 159647, April 15, 2005.

<sup>17</sup> Underscoring supplied; Citations omitted.



**CATHOLIC EDUCATIONAL  
ASSOCIATION OF THE PHILIPPINES**

**C. RELIEF SOUGHT**

In view of the foregoing, we respectfully request the withdrawal and/or amendment of RMO No. 20-2013 in order to comply with self-executory provisions of the Constitution and the Tax Code and the cessation of the implementation of the foregoing regulation.

We trust that our request will merit your usual favorable action and response.

Very truly yours,

**CATHOLIC EDUCATIONAL ASSOCIATION OF THE PHILIPPINES**

By:

**Br. Narciso S. Erguiza FSC (signed)**

President

Catholic Educational Association of the Philippines