

COMMISSIONER OF INTERNAL REVENUE, PETITIONER, VS. JOHN GOTAMCO & SONS, INC. AND THE COURT OF TAX APPEALS, RESPONDENTS.

G.R. No. L-31092. February 27, 1987

Ponente: YAP, J.

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YAP, J.:

The question involved in this petition is whether respondent John Gotamco & Sons, Inc. should pay the 3% contractor's tax under Section 191 of the National Internal Revenue Code on the gross receipts it realized from the construction of the World Health Organization office building in Manila.

The World Health Organization (WHO for short) is an international organization which has a regional office in Manila. As an international organization, it enjoys privileges and immunities which are defined more specifically in the Host Agreement entered into between the Republic of the Philippines and the said Organization on July 22, 1951. Section 11 of that Agreement provides, *inter alia*, that "the Organization, its assets, income and other properties shall be: (a) exempt from all direct and indirect taxes. It is understood, however, that the Organization will not claim exemption from taxes which are, in fact, no more than charges for public utility services; . . ."

When the WHO decided to construct a building to house its own offices, as well as the other United Nations offices stationed in Manila, it entered into a further agreement with the Government of the Republic of the Philippines on November 26, 1957. This agreement contained the following provision (Article III, paragraph 2):

"The Organization may import into the country materials and fixtures required for the construction free from all duties and taxes and agrees not to utilize any portion of the international reserves of the Government."

Article VIII of the above-mentioned agreement referred to the Host Agreement concluded on July 22, 1951 which granted the Organization exemption from all direct and indirect taxes.

In inviting bids for the construction of the building, the WHO informed the bidders that the building to be constructed belonged to an international organization with diplomatic status and thus exempt from the payment of all fees, licenses, and taxes, and that therefore their bids "must take this into account and should not include items for such taxes, licenses and other payments to Government agencies".

The construction contract was awarded to respondent John Gotamco & Sons, Inc. (Gotamco for short) on February 10, 1958 for the stipulated price of P370,000.00, but when the building was completed the price reached a total of P452,544.00.

Sometime in May 1958, the WHO received an opinion from the Commissioner of the Bureau of Internal Revenue stating that "as the 3% contractor's tax is an indirect tax on the assets and income of the Organization, the gross receipts derived by contractors from their contracts with the WHO for the construction of its new building, are exempt from tax in accordance with . . . the Host Agreement". Subsequently, however, on June 3, 1958, the Commissioner of Internal Revenue reversed his opinion and stated that "as the 3% contractor's tax is not a direct

nor an indirect tax on the WHO, but a tax that is primarily due from the contractor, the same is not covered by . . . the Host Agreement".

On January 2, 1960, the WHO issued a certification stating, *inter alia*,:

"When the request for bids for the construction of the World Health Organization office building was called for, contractors were informed that there would be no taxes or fees levied upon them for their work in connection with the construction of the building as this will be considered an indirect tax to the Organization caused by the increase of the contractor's bid in order to cover these taxes. This was upheld by the Bureau of Internal Revenue and it can be stated that the contractors submitted their bids in good faith with the exemption in mind.

The undersigned, therefore, certifies that the bid of John Gotamco & Sons, made under the condition stated above, should be exempted from any taxes in connection with the construction of the World Health Organization office building."

On January 17, 1961, the Commissioner of Internal Revenue sent a letter of demand to Gotamco demanding payment of P16,970.40, representing the 3% contractor's tax plus surcharges on the gross receipts it received from the WHO in the construction of the latter's building.

Respondent Gotamco appealed the Commissioner's decision to the Court of Tax Appeals, which after trial rendered a decision in favor of Gotamco and reversed the Commissioner's decision. The Court of Tax Appeal's decision is now before us for review on certiorari.

In his first assignment of error, petitioner questions the entitlement of the WHO to tax exemption, contending that the Host Agreement is null and void, not having been ratified by the Philippine Senate as required by the Constitution. We find no merit in this contention. While treaties are required to be ratified by the Senate under the Constitution, less formal types of international agreements may be entered into by the Chief Executive and become binding without the concurrence of the legislative body.[1] The Host Agreement comes within the latter category; it is a valid and binding international agreement even without the concurrence of the Philippine Senate. The privileges and immunities granted to the WHO under the Host Agreement have been recognized by this Court as legally binding on Philippine authorities.[2]

Petitioner maintains that even assuming that the Host Agreement granting tax exemption to the WHO is valid and enforceable, the 3% contractor's tax assessed on Gotamco is not an "indirect tax" within its purview. Petitioner's position is that the contractor's tax "is in the nature of an excise tax which is a charge imposed upon the performance of an act, the enjoyment of a privilege or the engaging in an occupation . . . It is a tax due primarily and directly on the contractor, not on the owner of the building. Since this tax has no bearing upon the WHO, it cannot be deemed an indirect taxation upon it."

We agree with the Court of Tax Appeals in rejecting this contention of the petitioner. Said the respondent court:

"In context, direct taxes are those that are demanded from the very person who, it is intended or desired, should pay them; while indirect taxes are those that are demanded in the first instance from one person in the expectation and intention that he can shift the burden to someone else. (Pollock vs. Farmers, L & T Co., 1957 US 429, 15 S. Ct. 673, 39 Law. Ed. 759.) The contractor's tax is of course payable by the contractor but in the last analysis it is the owner of the building that shoulders the burden of the tax because the same is shifted by the contractor to the owner as a matter of self-preservation. Thus, it is an indirect tax. And it is an indirect tax on the WHO because, although it is payable by the petitioner, the latter can shift its burden on the WHO. In the last analysis it is the WHO that will pay the tax indirectly through the contractor and it certainly cannot be said that 'this tax has no bearing upon the World Health Organization'."

Petitioner claims that under the authority of the Philippine Acetylene Company versus Commissioner of Internal Revenue, et al.,^[3] the 3% contractor's tax falls directly on Gotamco and cannot be shifted to the WHO. The Court of Tax Appeals, however, held that the said case is not controlling in this case, since the Host Agreement specifically exempts the WHO from "indirect taxes". We agree. The Philippine Acetylene case involved a tax on sales of goods which under the law had to be paid by the manufacturer or producer; the fact that the manufacturer or producer might have added the amount of the tax to the price of the goods did not make the sales tax "a tax on the purchaser". The Court held that the sales tax must be paid by the manufacturer or producer even if the sale is made to tax-exempt entities like the National Power Corporation, an agency of the Philippine Government, and to the Voice of America, an agency of the United States Government.

The Host Agreement, in specifically exempting the WHO from "indirect taxes", contemplates taxes which, although not imposed upon or paid by the Organization directly, form part of the price paid or to be paid by it. This is made clear in Section 12 of the Host Agreement which provides:

"While the Organization will not, as a general rule, in the case of minor purchases, claim exemption from excise duties, and from taxes on the sale of movable and immovable property which form part of the price to be paid, nevertheless, when the Organization is making important purchases for official use of property on which such duties and taxes have been charged or are chargeable the Government of the Republic of the Philippines shall make appropriate administrative arrangements for the remission or return of the amount of duty or tax." (Emphasis supplied).

The above-quoted provision, although referring only to purchases made by the WHO, elucidates the clear intention of the Agreement to exempt the WHO from "indirect" taxation.

The certification issued by the WHO, dated January 20, 1960, sought exemption of the contractor, Gotamco, from any taxes in connection with the construction of the WHO office building. The 3% contractor's tax would be within this category and should be viewed as a form of an "indirect tax" on the Organization, as the payment thereof or its inclusion in the bid price would have meant an increase in the construction cost of the building.

Accordingly, finding no reversible error committed by the respondent Court of Tax Appeals, the appealed decision is hereby affirmed.

SO ORDERED.

Narvasa, Melencio-Herrera, Cruz, Feliciano, Gancayco, and Sarmiento, JJ., concur.

[1] *Usaffe Veterans Association, Inc. vs. Treasurer of the Philippines, et al.*, 105 Phil. 1030.

[2] *World Health Organization and Dr. Leonce Verstuyft v. Hon. Benjamin Aquino, etc., et al.*, 48 SCRA 242.

[3] 127 Phil. 461.

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