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THIRD DIVISION

[G.R. No. 158085. October 14, 2005]

REPUBLIC OF THE PHILIPPINES, Represented by the COMMISSIONER OF INTERNAL REVENUE, *petitioner, vs.* **SUNLIFE ASSURANCE COMPANY OF CANADA,** *respondent*.

SYLLABUS

1. TAXATION; TAX CODE; ON COOPERATIVES; RESPONDENT IS A COOPERATIVE ENGAGED IN MUTUAL LIFE INSURANCE BUSINESS. — The Tax Code defines a cooperative as an association "conducted by the members thereof with the money collected from among themselves and solely for their own protection and not for profit." Without a doubt, respondent is a cooperative engaged in a mutual life insurance business. *First*, it is managed by its members. Both the CA and the CTA found that the management and affairs of respondent were conducted by its member-policyholders. x x x *Second*, it is operated with money collected from its members. Since respondent is composed entirely of members who are also its policyholders, all premiums collected obviously come only from them. x x x *Third*, it is licensed for the mutual protection of its members, not for the profit of anyone. x x x Verily, a mutual life insurance corporation is a cooperative that promotes the welfare of its own members. It does not operate for profit, but for the mutual benefit of its member-policyholders. They receive their insurance at cost, while reasonably and properly guarding and maintaining the stability and solvency of the company. "The economic benefits filter to the cooperative members. Either equally or proportionally, they are distributed among members in correlation with the resources of the association utilized."

2. COMMERCIAL LAW; INSURANCE; STOCK INSURANCE COMPANY MAY BE TRANSFORMED INTO A MUTUAL INSURANCE COMPANY; CASE AT BAR. — A stock insurance company doing business in the Philippines may "alter its organization and transform itself into a mutual insurance

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company." Respondent has been mutualized or converted from a stock life insurance company to a nonstock mutual life insurance corporation pursuant to Section 266 of the Insurance Code of 1978. On the basis of its bylaws, its ownership has been vested in its member-policyholders who are each entitled to one vote; and who, in turn, elect from among themselves the members of its board of trustees. Being the governing body of a nonstock corporation, the board exercises corporate powers, lays down all corporate business policies, and assumes responsibility for the efficiency of management. x x x The member-policyholders constitute "both insurer and insured" who "contribute, by a system of premiums or assessments, to the creation of a fund from which all losses and liabilities are paid." The premiums pooled into this fund are earmarked for the payment of their indemnity and benefit claims.

3. ID.; ID.; MUTUAL LIFE INSURANCE COMPANY; ELUCIDATED. — A mutual life insurance company is conducted for the benefit of its member-policyholders, who pay into its capital by way of premiums. To that extent, they are responsible for the payment of all its losses. "The cash paid in for premiums and the premium notes constitute their assets x x x." In the event that the company itself fails before the terms of the policies expire, the member-policyholders do not acquire the status of creditors. Rather, they simply become debtors for whatever premiums that they have originally agreed to pay the company, if they have not yet paid those amounts in full, for "[m]utual companies x x x depend solely upon x x x premiums." Only when the premiums will have accumulated to a sum larger than that required to pay for company losses will the member-policyholders be entitled to a "*pro rata* division thereof as profits." Contributing to its capital, the member-policyholders of a mutual company are obviously also its owners. Sustaining a dual relationship *inter se*, they not only contribute to the payment of its losses, but are also entitled to a proportionate share and participate alike in its profits and surplus.

4. ID.; ID.; ID.; LARGE RATES OF PREMIUMS CHARGED; ELUCIDATED. — Where the insurance is taken at cost, it is important that the rates of premium charged by a mutual company be larger than might reasonably be expected to carry the insurance, in order to constitute a margin of safety. The table of mortality used will show an admittedly higher death rate than will probably

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prevail; the assumed interest rate on the investments of the company is made lower than is expected to be realized; and the provision for contingencies and expenses, made greater than would ordinarily be necessary. This course of action is taken, because a mutual company has no capital stock and relies solely upon its premiums to meet unexpected losses, contingencies and expenses.

5. ID.; ID.; ID.; SHARING IN THE COMMON FUND; ELUCIDATED. — Certainly, many factors are considered in calculating the insurance premium. Since they vary with the kind of insurance taken and with the group of policyholders insured, any excess in the amount anticipated by a mutual company to cover the cost of providing for the insurance over its actual realized cost will also vary. If a member-policyholder receives an excess payment, then the apportionment must have been based upon a calculation of the actual cost of insurance that the company has provided for that particular member-policyholder. Accordingly, in apportioning divisible surpluses, any mutual company uses a contribution method that aims to distribute those surpluses among its member-policyholders, in the same proportion as they have contributed to the surpluses by their payments. Sharing in the common fund, any member-policyholder may choose to withdraw dividends in cash or to apply them in order to reduce a subsequent premium, purchase additional insurance, or accelerate the payment period. Although the premium made at the beginning of a year is more than necessary to provide for the cost of carrying the insurance, the member-policyholder will nevertheless receive the benefit of the overcharge by way of dividends, at the end of the year when the cost is actually ascertained. "The declaration of a dividend upon a policy reduces *pro tanto* the cost of insurance to the holder of the policy. That is its purpose and effect."

6. ID.; ID.; ID.; ID.; DIVIDEND RECEIVED BY MEMBER-POLICYHOLDERS; ELUCIDATED.— A stipulated insurance premium "cannot be increased, but may be lessened annually by so much as the experience of the preceding year has determined it to have been greater than the cost of carrying the insurance x x x." The difference between that premium and the cost of carrying the risk of loss constitutes the so-called "dividend" which, however, "is not in any real sense a dividend." It is a technical term that is well understood in the insurance business

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to be widely different from that to which it is ordinarily attached. The so-called "dividend" that is received by member-policyholders is not a portion of profits set aside for distribution to the stockholders in proportion to their subscription to the capital stock of a corporation. *One*, a mutual company has no capital stock to which subscription is necessary; there are no stockholders to speak of, but only members. And, *two*, the amount they receive does not partake of the nature of a profit or income. The quasi-appearance of profit will not change its character. It remains an *overpayment*, a benefit to which the member-policyholder is equitably entitled.

7. ID.; ID.; NONSTOCK CORPORATION; IN MAKING PROFIT AS ITS SECONDARY PURPOSE, IT MAY INVEST CORPORATE FUNDS TO EARN ADDITIONAL INCOME FOR ITS EXPENSES AND FOR FURTHERANCE OF THE ORGANIZATION'S PURPOSE. — It does not follow that because respondent is registered as a nonstock corporation and thus exists for a purpose other than profit, the company can no longer make any profits. Earning profits is merely its secondary, not primary, purpose. In fact, it may not lawfully engage in any business activity for profit, for to do so would change or contradict its nature as a non-profit entity. It may, however, invest its corporate funds in order to earn additional income for paying its operating expenses and meeting benefit claims. Any excess profit it obtains as an incident to its operations can only be used, whenever necessary or proper, for the furtherance of the purpose for which it was organized.

8. TAXATION; TAX CODE; COOPERATIVE; EXEMPTIONS; TO ENJOY EXEMPTIONS, REGISTRATION OF MUTUAL LIFE INSURANCE COMPANY WITH THE COOPERATIVE DEVELOPMENT AUTHORITY (CDA), NOT NECESSARY; REQUIREMENT THEREOF UNDER A REVENUE MEMORANDUM CIRCULAR CANNOT PREVAIL OVER ITS ABSENCE UNDER THE TAX CODE. — Under the Tax Code although respondent is a cooperative, registration with the Cooperative Development Authority (CDA) is not necessary in order for it to be exempt from the payment of both percentage taxes on insurance premiums, under Section 121; and documentary stamp taxes on policies of insurance or annuities it grants, under Section 199. x x x [T]he Tax Code does not require registration

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with the CDA. No tax provision requires a mutual life insurance company to register with that agency in order to enjoy exemption from both percentage and documentary stamp taxes. A provision of Section 8 of Revenue Memorandum Circular (RMC) No. 48-91 requires the submission of the Certificate of Registration with the CDA, before the issuance of a tax exemption certificate. That provision cannot prevail over the clear absence of an equivalent requirement under the Tax Code.

9. ID.; ID.; ID.; COOPERATIVE CODE OF THE PHILIPPINES DOES NOT APPLY. — x x x [T]he provisions of the Cooperative Code of the Philippines do not apply. x x x Respondent does not fall under any of the above-mentioned types of cooperatives required to be registered under PD 175. When the Cooperative Code was enacted years later, all cooperatives that were registered under PD 175 and previous laws were also deemed registered with the CDA. Since respondent was not required to be registered under the old law on cooperatives, it followed that it was not required to be registered even under the new law. Furthermore, only cooperatives to be formed or organized under the Cooperative Code needed registration with the CDA. Respondent already existed before the passage of the new law on cooperatives. It was not even required to organize under the Cooperative Code, not only because it performed a different set of functions, but also because it did not operate to serve the same objectives under the new law — particularly on productivity, marketing and credit extension.

10. ID.; ID.; ID.; EXEMPTION PROPER FOR RESPONDENT COOPERATIVE AS THE NATURE OF ITS OPERATION IS CLEAR AND ITS PURPOSE WELL-DEFINED. — We have already determined that respondent is a cooperative. The distinguishing feature of a cooperative enterprise is the mutuality of cooperation among its member-policyholders united for that purpose. So long as respondent meets this essential feature, it does not even have to use and carry the name of a cooperative to operate its mutual life insurance business. *Gratia argumenti* that registration is mandatory, it cannot deprive respondent of its tax exemption privilege merely because it failed to register. The nature of its operations is clear; its purpose well-defined. Exemption when granted cannot prevail over administrative convenience.

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11. ID.; ID.; ID.; PREMIUM TAXES AND DOCUMENTARY STAMP TAXES. — The Tax Code is clear. On the one hand, Section 121 of the Code exempts cooperative companies from the 5 percent percentage tax on insurance premiums. On the other hand, Section 199 also exempts from the DST, policies of insurance or annuities made or granted by cooperative companies. Being a cooperative, respondent is thus exempt from both types of taxes. It is worthy to note that while RA 8424 amending the Tax Code has deleted the income tax of 10 percent imposed upon the gross investment income of mutual life insurance companies — domestic and foreign — the provisions of Section 121 and 199 remain unchanged.

APPEARANCES OF COUNSEL

The Litigation Division (BIR) for petitioner.
Ma. Emeren V. Vallente for respondent.

D E C I S I O N

PANGANIBAN, *J.*:

Having satisfactorily proven to the Court of Tax Appeals, to the Court of Appeals and to this Court that it is a bona fide cooperative, respondent is entitled to exemption from the payment of taxes on life insurance premiums and documentary stamps. Not being governed by the Cooperative Code of the Philippines, it is not required to be registered with the Cooperative Development Authority in order to avail itself of the tax exemptions. Significantly, neither the Tax Code nor the Insurance Code mandates this administrative registration.

The Case

Before us is a Petition for Review[1] under Rule 45 of the Rules of Court, seeking to nullify the January 23, 2003 Decision[2] and the April 21, 2003 Resolution[3] of the Court of Appeals

[1] *Rollo*, pp. 7-32.

[2] *Id.*, pp. 37-44. Thirteenth Division. Penned by Justice Oswaldo D. Agcaoili (chair) and concurred in by Justices Eliezer R. de los Santos and Regalado E. Maambong (members).

[3] *Id.*, p. 46.

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(CA) in CA-GR SP No. 69125. The dispositive portion of the Decision reads as follows:

"WHEREFORE, the petition for review is hereby DENIED."[4]

The Facts

The antecedents, as narrated by the CA, are as follows:

"Sun Life is a mutual life insurance company organized and existing under the laws of Canada. It is registered and authorized by the Securities and Exchange Commission and the Insurance Commission to engage in business in the Philippines as a mutual life insurance company with principal office at Paseo de Roxas, Legaspi Village, Makati City.

"On October 20, 1997, Sun Life filed with the [Commissioner of Internal Revenue] (CIR) its insurance premium tax return for the third quarter of 1997 and paid the premium tax in the amount of ₱31,485,834.51. For the period covering August 21 to December 18, 1997, petitioner filed with the CIR its [documentary stamp tax (DST)] declaration returns and paid the total amount of ₱30,000,000.00.

"On December 29, 1997, the [Court of Tax Appeals] (CTA) rendered its decision in *Insular Life Assurance Co. Ltd. v. [CIR]*, which held that mutual life insurance companies are purely cooperative companies and are exempt from the payment of premium tax and DST. This pronouncement was later affirmed by this court in *[CIR] v. Insular Life Assurance Company, Ltd.* Sun Life surmised that[,] being a mutual life insurance company, it was likewise exempt from the payment of premium tax and DST. Hence, on August 20, 1999, Sun Life filed with the CIR an administrative claim for tax credit of its alleged erroneously paid premium tax and DST for the aforestated tax periods.

"For failure of the CIR to act upon the administrative claim for tax credit and with the 2-year period to file a claim for tax credit or refund dwindling away and about to expire, Sun Life filed with the CTA a petition for review on August 23, 1999. In its petition, it prayed for the issuance of a tax credit certificate in the amount of ₱61,485,834.51 representing ₱31,485,834.51 of erroneously paid premium tax for the third quarter of 1997 and ₱30,000[,000].00 of DST on policies of insurance from August 21 to December 18, 1997. Sun Life stood

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[4] CA Decision, p. 8; *rollo*, p. 44.

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firm on its contention that it is a mutual life insurance company vested with all the characteristic features and elements of a cooperative company or association as defined in [S]ection 121 of the Tax Code. Primarily, the management and affairs of Sun Life were conducted by its members; secondly, it is operated with money collected from its members; and, lastly, it has for its purpose the mutual protection of its members and not for profit or gain.

"In its answer, the CIR, then respondent, raised as special and affirmative defenses the following:

> '7. Petitioner's (Sun Life's) alleged claim for refund is subject to administrative routinary investigation/examination by respondent's (CIR's) Bureau.
>
> '8. Petitioner must prove that it falls under the exception provided for under Section 121 (now 123) of the Tax Code to be exempted from premium tax and be entitled to the refund sought.
>
> '9. Claims for tax refund/credit are construed strictly against the claimants thereof as they are in the nature of exemption from payment of tax.
>
> '10. In an action for tax credit/refund, the burden is upon the taxpayer to establish its right thereto, and failure to sustain this burden is fatal to said claim. x x x
>
> '11. It is incumbent upon petitioner to show that it has complied with the provisions of Section 204[,] in relation to Section 229, both in the 1997 Tax Code.'

"On November 12, 2002, the CTA found in favor of Sun Life. Quoting largely from its earlier findings in *Insular Life Assurance Company, Ltd. v. [CIR]*, which it found to be on all fours with the present action, the CTA ruled:

> 'The [CA] has already spoken. It ruled that a mutual life insurance company is a purely cooperative company[;] thus, exempted from the payment of premium and documentary stamp taxes. Petitioner Sun Life is without doubt a mutual life insurance company. x x x
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> x x x x x x x x x
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> 'Being similarly situated with Insular, Petitioner at bar is entitled to the same interpretation given by this Court in the

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earlier cases of *The Insular Life Assurance Company, Ltd. vs. [CIR]* (CTA Case Nos. 5336 and 5601) and by the [CA] in the case entitled *[CIR] vs. The Insular Life Assurance Company, Ltd.,* C.A. G.R. SP No. 46516, September 29, 1998. Petitioner Sun Life as a mutual life insurance company is[,] therefore[,] a cooperative company or association and is exempted from the payment of premium tax and [DST] on policies of insurance pursuant to Section 121 (now Section 123) and Section 199[1]) (now Section 199[a]) of the Tax Code.'

"Seeking reconsideration of the decision of the CTA, the CIR argued that Sun Life ought to have registered, foremost, with the Cooperative Development Authority before it could enjoy the exemptions from premium tax and DST extended to purely cooperative companies or associations under [S]ections 121 and 199 of the Tax Code. For its failure to register, it could not avail of the exemptions prayed for. Moreover, the CIR alleged that Sun Life failed to prove that ownership of the company was vested in its members who are entitled to vote and elect the Board of Trustees among [them]. The CIR further claimed that change in the 1997 Tax Code subjecting mutual life insurance companies to the regular corporate income tax rate reflected the legislature's recognition that these companies must be earning profits.

"Notwithstanding these arguments, the CTA denied the CIR's motion for reconsideration.

"Thwarted anew but nonetheless undaunted, the CIR comes to this court *via* this petition on the sole ground that:

> 'The Tax Court erred in granting the refund[,] because respondent does not fall under the exception provided for under Section 121 (now 123) of the Tax Code to be exempted from premium tax and DST and be entitled to the refund.'

"The CIR repleads the arguments it raised with the CTA and proposes further that the [CA] decision in *[CIR] v. Insular Life Assurance Company, Ltd.* is not controlling and cannot constitute *res judicata* in the present action. At best, the pronouncements are merely persuasive as the decisions of the Supreme Court alone have a universal and mandatory effect."[5]

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[5] *Id.,* pp. 1-4 & 37-40. Italics in the original.

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Ruling of the Court of Appeals

In upholding the CTA, the CA reasoned that respondent was a purely cooperative corporation duly licensed to engage in mutual life insurance business in the Philippines. Thus, respondent was deemed exempt from premium and documentary stamp taxes, because its affairs are managed and conducted by its members with money collected from among themselves, solely for their own protection, and not for profit. Its members or policyholders constituted both insurer and insured who contribute, by a system of premiums or assessments, to the creation of a fund from which all losses and liabilities were paid. The dividends it distributed to them were not profits, but returns of amounts that had been overcharged them for insurance.

For having satisfactorily shown with substantial evidence that it had erroneously paid and seasonably filed its claim for premium and documentary stamp taxes, respondent was entitled to a refund, the CA ruled.

Hence, this Petition.[6]

The Issues

Petitioner raises the following issues for our consideration:

"I.

"Whether or not respondent is a purely cooperative company or association under Section 121 of the National Internal Revenue Code and a fraternal or beneficiary society, order or cooperative company on the lodge system or local cooperation plan and organized and conducted solely by the members thereof for the exclusive benefit of each member and not for profit under Section 199 of the National Internal Revenue Code.

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[6] This case was deemed submitted for decision on April 1, 2005, upon this Court's receipt of petitioner's Memorandum, signed by Assistant Solicitor General Nestor J. Ballacillo and Associate Solicitor Raymond Joseph G. Javier. Respondent's Memorandum, signed by Atty. Ma. Emeren V. Vallente, was received by this Court on December 6, 2004.

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"II.

"Whether or not registration with the Cooperative Development Authority is a *sine qua non* requirement to be entitled to tax exemption.

"III.

"Whether or not respondent is exempted from payment of tax on life insurance premiums and documentary stamp tax."[7]

We shall tackle the issues *seriatim*.

The Court's Ruling

The Petition has no merit.

First Issue:

Whether Respondent Is a Cooperative

The Tax Code defines a cooperative as an association "conducted by the members thereof with the money collected from among themselves and solely for their own protection and not for profit."[8] Without a doubt, respondent is a cooperative engaged in a mutual life insurance business.

First, it is managed by its members. Both the CA and the CTA found that the management and affairs of respondent were conducted by its member-policyholders.[9]

A stock insurance company doing business in the Philippines may "alter its organization and transform itself into a mutual insurance company."[10] Respondent has been mutualized or converted from a stock life insurance company to a nonstock

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[7] Petitioner's Memorandum, p. 11; *rollo*, p. 384. Original in uppercase.

[8] §121 of the National Internal Revenue Code prior to its amendment by RA 8424.

[9] CA Decision, p. 6; *rollo*, p. 42; and CTA Decision, p. 7; *rollo*, p. 57.

The affairs of mutual companies "are managed by the policyholders." *Ohio Farmers Indemnity Co. v. Commissioner of Internal Revenue*, 108 F 2d 665, 667, January 15, 1940, per Hamilton, Circuit J.

[10] Last paragraph of §188 of the Insurance Code of 1978.

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mutual life insurance corporation[11] pursuant to Section 266 of the Insurance Code of 1978.[12] On the basis of its bylaws, its ownership has been vested in its member-policyholders who are each entitled to one vote;[13] and who, in turn, elect from among themselves the members of its board of trustees.[14] Being the governing body of a nonstock corporation, the board exercises corporate powers, lays down all corporate business policies, and assumes responsibility for the efficiency of management.[15]

Second, it is operated with money collected from its members. Since respondent is composed entirely of members who are also its policyholders, all premiums collected obviously come only from them.[16]

The member-policyholders constitute "both insurer and insured"[17] who "contribute, by a system of premiums or assessments, to the creation of a fund from which all losses and liabilities are paid."[18] The premiums[19] pooled into this fund are earmarked for the payment of their indemnity and benefit claims.

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[11] Art. 7 of respondent's Amended Articles of Incorporation.

[12] Presidential Decree (PD) No. 1460.

[13] "Unless so limited, broadened or denied, each member, regardless of class, shall be entitled to one vote." 1st paragraph of §89 of Batas Pambansa (BP) Blg. 68, otherwise known as "The Corporation Code of the Philippines."

[14] "No person shall be elected as trustee unless he is a member of the corporation." 2nd paragraph of §92 of BP 68.

[15] Campos Jr. & Campos, *The Corporation Code: Comments, Notes and Selected Cases*, Vol. I (1990), p. 340.

[16] CA Decision, p. 6; *rollo*, p. 42; and CTA Decision, p. 7; *rollo*, p. 57.

[17] *Keehn v. Hodge Drive-It-Yourself, Inc.*, 53 NE 2d 69, 71, July 19, 1943, per Hildebrant, *J.*

[18] *Minnick v. State Farm Mutual Automobile Insurance Co.*, 174 A 2d 706, 709, October 9, 1961, per Storey, *J.*

[19] A premium is the agreed price for assuming and carrying the risk of insurance. De Leon, *The Law on Insurance (with Insolvency Law)*, 10th ed. (2003), p. 114.

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Third, it is licensed for the mutual protection of its members, not for the profit of anyone.

As early as October 30, 1947, the director of commerce had already issued a license to respondent — a corporation organized and existing under the laws of Canada — to engage in business in the Philippines.[20] Pursuant to Section 225 of Canada's Insurance Companies Act, the Canadian minister of state (for finance and privatization) also declared in its Amending Letters Patent that respondent would be a mutual company effective June 1, 1992.[21] In the Philippines, the insurance commissioner also granted it annual Certificates of Authority to transact life insurance business, the most relevant of which were dated July 1, 1997 and July 1, 1998.[22]

A mutual life insurance company is conducted for the benefit of its member-policyholders,[23] who pay into its capital by way of premiums. To that extent, they are responsible for the payment of all its losses.[24] "The cash paid in for premiums and the premium notes constitute their assets x x x"[25] In the event that the company itself fails before the terms of the policies expire, the member-policyholders do not acquire the status of creditors.[26] Rather, they simply become debtors for whatever premiums that they have originally agreed to pay the company, if they have not yet paid those amounts in full, for "[m]utual companies x x x depend solely upon x x x premiums."[27] Only when the

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[20] *Rollo,* p. 97.

[21] *Id.,* p. 210.

[22] *Id.,* pp. 98-99.

[23] *Public Housing Administration v. Housing Authority of Bogalusa,* 137 So. 2d 315, 321, February 19, 1962.

[24] *Ibid.*

[25] *Gleason v. Prudential Fire Insurance Co.,* 151 SW 1030, 1033, December 19, 1912, per Green, *J.*

[26] *Public Housing Administration v. Housing Authority of Bogalusa, supra.*

[27] *Ohio Farmers Indemnity Co. v. Commissioner of Internal Revenue, supra.*

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premiums will have accumulated to a sum larger than that required to pay for company losses will the member-policyholders be entitled to a "*pro rata* division thereof as profits."[28]

Contributing to its capital, the member-policyholders of a mutual company are obviously also its owners.[29] Sustaining a dual relationship *inter se*, they not only contribute to the payment of its losses, but are also entitled to a proportionate share[30] and participate alike[31] in its profits and surplus.

Where the insurance is taken at cost, it is important that the rates of premium charged by a mutual company be larger than might reasonably be expected to carry the insurance, in order to constitute a margin of safety. The table of mortality used will show an admittedly higher death rate than will probably prevail; the assumed interest rate on the investments of the company is made lower than is expected to be realized; and the provision for contingencies and expenses, made greater than would ordinarily be necessary.[32] This course of action is taken, because a mutual company has no capital stock and relies solely upon its premiums to meet unexpected losses, contingencies and expenses.

Certainly, many factors are considered in calculating the insurance premium. Since they vary with the kind of insurance taken and with the group of policyholders insured, any excess in the amount anticipated by a mutual company to cover the cost of providing for the insurance over its actual realized cost will also vary. If a member-policyholder receives an excess payment, then the apportionment must have been based upon a calculation of the actual cost of insurance that the company

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[28] *Public Housing Administration v. Housing Authority of Bogalusa, supra,* per McCaleb, *J.*

[29] *Ibid*.

[30] *Keehn v. Hodge Drive-It-Yourself, Inc., supra.*

[31] *Ohio Farmers Indemnity Co. v. Commissioner of Internal Revenue, supra.*

[32] *Mutual Benefit Life Insurance Co. v. Herold*, 198 F 199, 204, July 29, 1912.

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has provided for that particular member-policyholder. Accordingly, in apportioning divisible surpluses, any mutual company uses a contribution method that aims to distribute those surpluses among its member-policyholders, in the same proportion as they have contributed to the surpluses by their payments.[33]

Sharing in the common fund, any member-policyholder may choose to withdraw dividends in cash or to apply them in order to reduce a subsequent premium, purchase additional insurance, or accelerate the payment period. Although the premium made at the beginning of a year is more than necessary to provide for the cost of carrying the insurance, the member-policyholder will nevertheless receive the benefit of the overcharge by way of dividends, at the end of the year when the cost is actually ascertained. "The declaration of a dividend upon a policy reduces *pro tanto* the cost of insurance to the holder of the policy. That is its purpose and effect."[34]

A stipulated insurance premium "cannot be increased, but may be lessened annually by so much as the experience of the preceding year has determined it to have been greater than the cost of carrying the insurance x x x."[35] The difference between that premium and the cost of carrying the risk of loss constitutes the so-called "dividend" which, however, "is not in any real sense a dividend."[36] It is a technical term that is well understood in the insurance business to be widely different from that to which it is ordinarily attached.

The so-called "dividend" that is received by member-policyholders is not a portion of profits set aside for distribution to the stockholders in proportion to their subscription to the

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[33] *Rhine v. New York Life Insurance Co.*, 6 NE 2d 74, 76-77, December 31, 1936.

[34] *Id*., p. 78, December 31, 1936, per Lehman, *J*.

[35] *Mutual Benefit Life Insurance Co. v. Herold, id.*, 204-205, per Cross, District *J*.

[36] *Ibid*.

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capital stock of a corporation.[37] *One,* a mutual company has no capital stock to which subscription is necessary; there are no stockholders to speak of, but only members. And, *two,* the amount they receive does not partake of the nature of a profit or income. The quasi-appearance of profit will not change its character. It remains an *overpayment,* a benefit to which the member-policyholder is equitably entitled.[38]

Verily, a mutual life insurance corporation is a cooperative that promotes the welfare of its own members. It does not operate for profit, but for the mutual benefit of its member-policyholders. They receive their insurance at cost, while reasonably and properly guarding and maintaining the stability and solvency of the company.[39] "The economic benefits filter to the cooperative members. Either equally or proportionally, they are distributed among members in correlation with the resources of the association utilized."[40]

It does not follow that because respondent is registered as a nonstock corporation and thus exists for a purpose other than profit, the company can no longer make any profits.[41] Earning profits is merely its secondary, not primary, purpose. In fact, it may not lawfully engage in any business activity for profit, for to do so would change or contradict its nature[42] as a non-profit entity.[43] It may, however, invest its corporate funds in order to earn additional income for paying its operating expenses and meeting benefit claims. Any excess profit it obtains as an

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[37] Campos Jr. & Campos, *The Corporation Code: Comments, Notes and Selected Cases,* Vol. II (1990), p. 209.

[38] *Mutual Benefit Life Insurance Co. v. Herold, supra.*

[39] *Ibid*.

[40] *Nueva Ecija I Electric Cooperative, Inc. v. NLRC,* 380 Phil. 44, 58, January 24, 2000, per Quisumbing, *J*.

[41] Campos Jr. & Campos, *The Corporation Code: Comments, Notes and Selected Cases,* Vol. I (1990), p. 44.

[42] §14(2) of BP 68.

[43] De Leon, *The Law on Partnerships and Private Corporations* (1985), p. 401.

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incident to its operations can only be used, whenever necessary or proper, for the furtherance of the purpose for which it was organized.[44]

Second Issue:

Whether CDA Registration Is Necessary

Under the Tax Code although respondent is a cooperative, registration with the Cooperative Development Authority (CDA)[45] is not necessary in order for it to be exempt from the payment of both percentage taxes on insurance premiums, under Section 121; and documentary stamp taxes on policies of insurance or annuities it grants, under Section 199.

First, the Tax Code does not require registration with the CDA. No tax provision requires a mutual life insurance company to register with that agency in order to enjoy exemption from both percentage and documentary stamp taxes.

A provision of Section 8 of Revenue Memorandum Circular (RMC) No. 48-91 requires the submission of the Certificate of Registration with the CDA,[46] before the issuance of a tax exemption certificate. That provision cannot prevail over the clear absence of an equivalent requirement under the Tax Code. *One,* as we will explain below, the Circular does not apply to respondent, but only to cooperatives that need to be registered under the Cooperative Code. *Two,* it is a mere issuance directing all internal revenue officers to publicize a new tax legislation. Although the Circular does not derogate from their authority to implement the law, it cannot add a registration requirement,[47] when there is none under the law to begin with.

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[44] 1st paragraph of §87 of BP 68.

[45] The Cooperative Development Authority (CDA) is created under RA 6939. *Camarines Norte Electric Cooperative, Inc. v. Torres,* 350 Phil. 315, 318, February 27, 1998.

[46] §8.1.b of Revenue Memorandum Circular (RMC) No. 48-91.

[47] De Leon, *The Fundamentals of Taxation* (12th ed., 1998), pp. 81-82.

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Second, the provisions of the Cooperative Code of the Philippines[48] do not apply. Let us trace the Code's development in our history.

As early as 1917, a cooperative company or association was already defined as one "conducted by the members thereof with money collected from among themselves and solely for their own protection and not profit."[49] In 1990, it was further defined by the Cooperative Code as a "duly registered association of persons, with a common bond of interest, who have voluntarily joined together to achieve a lawful common social or economic end, making equitable contributions to the capital required and accepting a fair share of the risks and benefits of the undertaking in accordance with universally accepted cooperative principles."[50]

The Cooperative Code was actually an offshoot of the old law on cooperatives. In 1973, Presidential Decree (PD) No. 175 was signed into law by then President Ferdinand E. Marcos in order to strengthen the cooperative movement.[51] The promotion of cooperative development was one of the major programs of the "New Society" under his administration. It sought to improve the country's trade and commerce by enhancing agricultural production, cottage industries, community development, and agrarian reform through cooperatives.[52]

The whole cooperative system, with its vertical and horizontal linkages — from the market cooperative of agricultural products to cooperative rural banks, consumer cooperatives and

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[48] On 10 March 1990, then President Corazon C. Aquino has signed into law Republic Act (RA) No. 6938, otherwise known as "The Cooperative Code of the Philippines. *Camarines Norte Electric Cooperative, Inc. v. Torres, supra.*

[49] *La Compañia General de Tabacos de Filipinas v. Collector of Internal Revenue*, 48 Phil. 35, 44, September 26, 1925, per Johns, *J.* (citing §1505 of the Administrative Code of 1917).

[50] Art. 3 of Republic Act (RA) No. 6938.

[51] *Cooperative Rural Bank of Davao City, Inc. v. Ferrer-Calleja*, 165 SCRA 725, 732, September 26, 1988, per Gancayco, *J.*

[52] Fajardo & Abella, *Cooperative (Kilusang Bayan)*, 1981, p. 211.

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cooperative insurance — was envisioned to offer considerable economic opportunities to people who joined cooperatives.[53] As an effective instrument in redistributing income and wealth,[54] cooperatives were promoted primarily to support the agrarian reform program of the government.[55]

Notably, the cooperative under PD 175 referred only to an organization composed primarily of small producers and consumers who voluntarily joined to form a business enterprise that they themselves owned, controlled, and patronized.[56] The Bureau of Cooperatives Development — under the Department of Local Government and Community Development (later Ministry of Agriculture)[57] — had the authority to register, regulate and supervise only the following cooperatives: (1) *barrio* associations involved in the issuance of certificates of land transfer; (2) local or primary cooperatives composed of natural persons and/or *barrio* associations; (3) federations composed of cooperatives that may or may not perform business activities; and (4) unions of cooperatives that did not perform any business activities.[58] Respondent does not fall under any of the above-mentioned types of cooperatives required to be registered under PD 175.

When the Cooperative Code was enacted years later, all cooperatives that were registered under PD 175 and previous laws were also deemed registered with the CDA.[59] Since respondent was not required to be registered under the old law on cooperatives, it followed that it was not required to be registered even under the new law.

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[53] *Id*., p. 213.

[54] §1 of Presidential Decree (PD) No. 175.

[55] Fajardo & Abella, *Cooperative (Kilusang Bayan)*; *id*., pp. 27 & 212; and 1st paragraph of the Foreword of Clemente E. Terso Jr., CESO II, director of the Bureau of Cooperatives Development.

[56] §2 of PD 175.

[57] Effective May 1, 1980. Fajardo & Abella, *Cooperative (Kilusang Bayan)*; *id.*, p. 27.

[58] Items 1 to 4 of §8(b) of PD 175.

[59] Art. 128 of RA 6938.

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Furthermore, only cooperatives to be formed or organized under the Cooperative Code needed registration with the CDA.[60] Respondent already existed before the passage of the new law on cooperatives. It was not even required to organize under the Cooperative Code, not only because it performed a different set of functions, but also because it did not operate to serve the same objectives under the new law — particularly on productivity, marketing and credit extension.[61]

The insurance against losses of the members of a cooperative referred to in Article 6(7) of the Cooperative Code is not the same as the life insurance provided by respondent to member-policyholders. The former is a function of a service cooperative,[62] the latter is not. Cooperative insurance under the Code is limited in scope and local in character. It is not the same as mutual life insurance.

We have already determined that respondent is a cooperative. The distinguishing feature of a cooperative enterprise[63] is the mutuality of cooperation among its member-policyholders united for that purpose.[64] So long as respondent meets this essential feature, it does not even have to use[65] and carry the name of a cooperative to operate its mutual life insurance business. *Gratia argumenti* that registration is mandatory, it cannot deprive respondent of its tax exemption privilege merely because it failed to register. The nature of its operations is clear; its purpose well-defined. Exemption when granted cannot prevail over administrative convenience.

Third, not even the Insurance Code requires registration with the CDA. The provisions of this Code primarily govern insurance contracts; only if a particular matter in question is not specifically

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[60] Art. 16 of RA 6938.

[61] Art. 7 of RA 6938.

[62] Art. 23(e) of RA 6938.

[63] *Minnick v. State Farm Mutual Automobile Insurance Co., supra.*

[64] *Ohio Farmers Indemnity Co. v. Commissioner of Internal Revenue, supra.*

[65] Art. 124(1) of RA 6938.

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provided for shall the provisions of the Civil Code on contracts and special laws govern.[66]

True, the provisions of the Insurance Code relative to the organization and operation of an insurance company also apply to cooperative insurance entities organized under the Cooperative Code.[67] The latter law, however, does not apply to respondent, which already existed as a cooperative company engaged in mutual life insurance prior to the laws passage of that law. The statutes prevailing at the time of its organization and mutualization were the Insurance Code and the Corporation Code, which imposed no registration requirement with the CDA.

Third Issue:

Whether Respondent Is Exempted

from Premium Taxes and DST

Having determined that respondent is a cooperative that does not have to be registered with the CDA, we hold that it is entitled to exemption from both premium taxes and documentary stamp taxes (DST).

The Tax Code is clear. On the one hand, Section 121 of the Code exempts cooperative companies from the 5 percent percentage tax on insurance premiums. On the other hand, Section 199 also exempts from the DST, policies of insurance or annuities made or granted by cooperative companies. Being a cooperative, respondent is thus exempt from both types of taxes.

It is worthy to note that while RA 8424 amending the Tax Code has deleted the income tax of 10 percent imposed upon the gross investment income of mutual life insurance companies — domestic[68] and foreign[69] — the provisions of Section 121 and 199 remain unchanged.[70]

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[66] *De Leon, The Law on Insurance (with Insolvency Law); id.*, p. 1.

[67] Art. 117 of RA 6938.

[68] §24(d) of the Tax Code.

[69] §25(a)(3) of the Tax Code.

[70] In fact, §9 of RA 9243, signed into law by President Gloria Macapagal-Arroyo only on February 17, 2004, retains §199(a) of the Tax Code.

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Having been seasonably filed and amply substantiated, the claim for exemption in the amount of ₱61,485,834.51, representing percentage taxes on insurance premiums and documentary stamp taxes on policies of insurance or annuities that were paid by respondent in 1997, is in order. Thus, the grant of a tax credit certificate to respondent as ordered by the appellate court was correct.

WHEREFORE, the Petition is hereby *DENIED*, and the assailed Decision and Resolution are *AFFIRMED*. No pronouncement as to costs.

SO ORDERED.

Sandoval-Gutierrez, Corona, Carpio Morales, and *Garcia, JJ.,* concur.

THIRD DIVISION

[G.R. No. 159831. October 14, 2005]

PILIPINAS SHELL PETROLEUM CORPORATION, *petitioner, vs.* **JOHN BORDMAN LTD. OF ILOILO, INC.,** *respondent.*

SYLLABUS

1. REMEDIAL LAW; CIVIL PROCEDURE; FORUM SHOPPING; VERIFICATION AND CERTIFICATION; CONFERRED POWER TO INSTITUTE ACTION INCLUDES POWER TO EXECUTE VERIFICATION AND CERTIFICATION AGAINST FORUM SHOPPING. — [P]etitioner's president conferred upon its vice-president the power to institute actions. As certified by the assistant board secretary, the delegation was authorized by petitioner's board of directors. The power to institute actions necessarily included the power to execute the