Republic of the Philippines
COURT OF TAX APPEALS
Quezon City

SPECIAL SECOND DIVISION

ST. LUKE'S MEDICAL CENTER, INC.,
Petitioner,

-versus-

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

CTA Case No. 7823
For: Assessment for Deficiency Income Tax for taxable years 2003 and 2004

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ST. LUKE'S MEDICAL CENTER, INC.,
Petitioner,

-versus-

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

CTA CASE NO. 7832
For: Assessment for Deficiency Income Tax, Value-Added Tax, Withholding Tax on Compensation, Expanded Withholding Tax and Documentary Stamp Tax for Taxable Year 2004

Members:
CASTAÑEDA, JR., Chairperson
CASANOVA, and
MINDARO-GRULLA, JJ.

Promulgated: FEB 18 2014

8:05 a.m.

x- x

D E C I S I O N

MINDARO-GRULLA, J.:

These are consolidated cases of two (2) Petitions for Review, docketed as CTA Case No. 7823 and CTA Case No. 7832, separately filed by St. Luke's Medical Center, Inc. as petitioner, against the Commissioner of Internal Revenue as respondent, for the Court in Division pursuant to Rule 7(a)(2) of Republic Act (RA) No. 1125, An Act Creating the Court of Tax Appeals, as amended[1], as well as Rule 4,

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1 Sec. 7. *Jurisdiction.* –The CTA shall exercise:
(a) Exclusive appellate jurisdiction to review by appeal, as herein provided:

x x x x x x

(2) Inaction by the Commissioner of Internal Revenue in cases involving disputed assessments, refunds or internal revenue taxes, fees or other charges, penalties in relation thereto, or other matters arising under the

Section 3 (a) (2), in relation to Rule 8, Section 4(a), of the Revised Rules of the Court of Tax Appeals (RRCTA)[2].

These consolidated cases, specifically, involve the appeal on the inaction of the Commissioner of Internal Revenue, relative to petitioner's protest against the issued assessments for alleged deficiency income tax, deficiency value-added tax (VAT), deficiency withholding tax on compensation, deficiency expanded withholding tax (EWT), and deficiency documentary stamp tax (DST) for the taxable

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National Internal Revenue Code or other laws administered by the Bureau of Internal Revenue, where the National Internal Revenue Code provides a specific period for action, in which the case the inaction shall be deemed a denial;

x x x x x x

2 Rule 4. Sec. 3. *Cases within the jurisdiction of the Court in Division.* – The Court in Division shall exercise:

(a) Exclusive original over or appellate jurisdiction to review by appeal the following:

x x x x x x

(2) Inaction by the Commissioner of Internal Revenue in cases involving disputed assessments, refunds of internal revenue taxes, fees or other charges, penalties in relation thereto, or other matters arising under the National Internal Revenue Code or other laws administered by the Bureau of Internal Revenue, where the National Internal Revenue Code or other applicable law provides a specific period for action: *Provided,* that in case of disputed assessments, the inaction of the Commissioner of Internal Revenue within the one hundred eighty day-period under Section 228 of the National Internal Revenue Code shall be deemed a denial for purposes of allowing the taxpayer to appeal his case to the Court and does not necessarily constitute a formal decision of the Commissioner of Internal Revenue on the tax case; *Provided, further,* that should the taxpayer opt to await the final decision of the Commissioner of Internal Revenue on the disputed assessments beyond the one hundred eighty day-period abovementioned, the taxpayer may appeal such final decision to the Court under Section 3(a), Rule 8 of these Rules; and *Provided, still further,* that in the case of claims for refund of taxes erroneously or illegally collected, the taxpayer must file a petition for review with the Court prior to the expiration of the two-year period under Section 229 of the National Internal Revenue Code;

x x x x x x

Rule 8. Sec. 4. *Where to appeal; mode of appeal.* –

(a) An Appeal from a decision or ruling or the inaction of the Commissioner of Internal Revenue on disputed assessments or claim for refund of internal revenue taxes erroneously or illegally collected; the decision or ruling of the Commissioner of Customs, the Secretary of Finance, the Secretary of Trade & Industry, the Secretary of Agriculture, and the Regional Trial Court in the exercise of their original jurisdiction, shall be taken to the Court by filing before it a petition for review as provided in Rule 42 of the Rules of Court. The Court in Division shall act on the appeal.

years 2003 and 2004, in the aggregate amount of ₱519,764,198.95, broken down as follows:

	Basic	Interest	Surcharge	Compromise	Total
CTA Case No. 7823					
Income Tax (2003)	P 49,443,736.00	P 35,870,414.50	P 12,360,934.00	P 25,000.00	P 97,700,084.50
Income Tax (2004)	75,932,647.20	39,901,045.84	18,983,161.80	25,000.00	134,841,854.84
Subtotal					*232,541,939.34*
CTA Case No. 7832	**Basic**	**Interest**	**Surcharge**	**Compromise**	**Total**
Income Tax	P 153,721,842.60	P 83,332,681.06		P 25,000.00	P 237,079,523.66
Value-added Tax	691,062.64	405,391.86		20,000.00	1,116,454.50
Withholding Tax on Compensation	19,764,533.96	11,756,738.99		25,000.00	31,546,272.95
Expanded Withholding Tax	10,706,598.01	6,368,714.73		66,000.00	17,141,312.74
Documentary Stamp Tax	174,918.00	104,048.26	43,729.50	16,000.00	338,695.76
Subtotal					*287,222,259.61*
TOTAL	**P310,435,338.41**	**P177,739,035.24**	**P31,387,825.30**	**P202,000.00**	**P519,764,198.95**

Petitioner is a non-stock, non-profit corporation duly organized and existing under Philippine laws, with address at 279 E. Rodriguez Sr. Blvd., Cathedral Heights, Quezon City. Petitioner has registered itself as a value-added taxpayer and was issued TIN/VAT No. 000-684-591.[3]

Respondent is the duly appointed Commissioner of the Bureau of Internal Revenue (BIR) vested with authority to exercise the functions of said office, including, *inter alia*, the power to abate or cancel a tax liability when the tax or any portion thereof appears to be unjustly or excessively assessed. She holds office at the BIR National Office Building, Diliman, Quezon City.

Petitioner received from the BIR Large Taxpayers Service-Document Processing and Quality Assurance Division Audit Results/Assessment Notice No. QA-07-000094 and Audit Results/Assessment Notice No. QA-07-000095 both dated November 22, 2007, assessing petitioner for deficiency income tax in the amount of ₱97,700,084.50 for the taxable year 2003 and in the amount of ₱134,841,854.84 for the taxable year 2004, respectively, or a total deficiency income tax of ₱232,541,939.34.[4]

[3] Pars. 1 and 2, Amended Joint Stipulation of Facts and Simplification of Issues, Docket, pp. 202-203.
[4] Par. 4, Amended Joint Stipulation of Facts and Simplification of Issues, Docket, p. 203.

Petitioner filed an administrative protest against the above-mentioned deficiency tax assessment on January 14, 2008, praying for its cancellation.[5]

Petitioner also received from the BIR Large Taxpayers Service an undated Formal Letter of Demand and Details of Discrepancies, with attached Assessment Notices, assessing petitioner for a total deficiency tax of ₱287,222,259.61 for the taxable year 2004; detailed as follows:

1. Audit Result/Assessment Notice No. INC-04-000205 for deficiency income tax amounting to ₱237,079,523.66;
2. Audit Result/Assessment Notice No. VT-04-000246 for deficiency VAT amounting to ₱1,116,454.50;
3. Audit Result/Assessment Notice No. WC-04-000105 for deficiency withholding tax on compensation amounting to ₱31,546,272.95;
4. Audit Result/Assessment Notice No. EWT-04-000195 for deficiency expanded withholding tax amounting to ₱17,141,312.72; and
5. Audit Result/Assessment Notice No. DST-04-000162 for deficiency documentary stamp tax amounting to ₱338,695.76.[6]

On February 20, 2008, petitioner filed an administrative protest against the enumerated deficiency tax assessments.

Due to respondent's inaction on petitioner's protests within the prescribed period of one hundred eighty (180) days, in accordance with Section 228 of the National Internal Revenue Code (NIRC) of 1997, as amended, petitioner filed two (2) separate Petitions for Review docketed as CTA Case Nos. 7823 and 7832 on August 12, 2008 and September 18, 2008, respectively.

Upon motion of petitioner[7], the two (2) cases were consolidated on December 11, 2008.[8]

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[5] Par. 13, Amended Joint Stipulation of Facts and Simplification of Issues, Docket, p. 205.
[6] Par. 22, Amended Joint Stipulation of Facts and Simplification of Issues, Docket, p. 208.

Respondent interposed the following Special and Affirmative Defenses in her Answers to the Petitions for Review docketed as CTA Case Nos. 7823[9] and 7832[10]:

CTA CASE NO. 7823

"5. The petitioner's assessment for deficiency income tax during the taxable year 2003 was made within the required three-year prescriptive period and in accordance with law and regulations.

6. Respondent maintains that petitioner St. Luke's Medical Center, Inc. is liable for deficiency income tax for taxable years 2003 and 2004 pursuant to Section 27 (B) of the 1997 National Internal Revenue Code (1997 NIRC), which states, *viz:*

> Section 27. Rates on Income Tax on Domestic Corporation.
>
> xxx xxx xxx
>
> (B) *Proprietary Educational Institutions and Hospitals.* – Proprietary educational institutions and ***hospitals which are nonprofit shall pay a tax of ten percent (10%) on their taxable income*** except those covered by Subsection (D) hereof: *Provided*, that if the gross income from unrelated trade, business or other activity exceeds fifty percent (50%) of the total gross income derived by such educational institutions or hospitals from all sources, the tax prescribed in Subsection (A) hereof shall be imposed on the entire taxable income. For the purposes of this Subsection, the term 'unrelated trade, business or other activity' means any trade, business or other activity, the conduct of which is not substantially related to the exercise or

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[7] Motion to Consolidate, Docket, pp. 188-194.
[8] Docket, p. 197.
[9] Docket, pp. 126-131.
[10] Answer (CTA Case No. 7832), pp. 3-28.

> performance by such educational institution or hospital of its primary purpose or function. A '*Proprietary educational institution*' is any private school maintained and administered by private individuals or groups with an issued permit to operate from the Department of Education, Culture and Sports (DECS), or the Commission on Higher Education (CHED), or the Technical Education and Skills Development Authority (TESDA), as the case may be, in accordance with existing laws and regulations.' (emphasis supplied)

7. Based from the above-quoted provision of Section 27 (B) of the 1997 NIRC, petitioner is subject to a preferential rate of 10% of its income tax for the years 2003 and 2004 considering that it falls under the category of hospital which is a non-profit.

8. On the other hand, petitioner's reliance of Section 30 (E) of the 1997 NIRC for tax exemption is utterly misplaced.

> 'SEC. 30. *Exemptions from Tax on Corporations*. – The following organizations shall not be taxed under this Title in respect to income received by them as such:
>
> xxx xxx xxx
>
> (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 inures to the benefit of any member, organizer, officer or any specific person.
>
> xxx xxx xxx
>
> (G) Civic league or organization not organized for profit but operated exclusively for the promotion of social welfare.'

9. Respondent submits that petitioner does not fall under the category of tax-exempt corporations within the purview of Section 30 of the 1997 NIRC on

the ground that it is not organized or operated exclusively for charitable and social welfare purposes and the fact that the net income of petitioner inures to the benefit of its members.

10. In fact upon perusal of the petitioner's Annual Income Tax Return (BIR Form No. 1702) for the year ending December 31, 2003 attached as Annex 'G' of the Petition for Review particularly under the items of nature of expense/deduction (page 3 of BIR Form No. 1972) indubitably shows that the item <u>*charitable contributions has* zero amount</u> while the other items thereof such as <u>salaries and *allowances*, anniversary *and* separation benefits show the amount of ₱91,*867*,139.00, ₱16,204,282.00 *and* ₱24,*263*,668.*00*</u> respectively and these amounts constitute the bulk of the expense and deduction account. This would only indicate that petitioner is not established or organized exclusively for charitable purposes but also for profit and majority of its income inures to the benefits of its members. *RES IPSA LOQUITUR*. (emphasis and underlining ours)

11. It is axiomatic that where the language of the law is clear and unambiguous, its express terms must be applied. Parenthetically, a consideration of the question of construction must not even begin, particularly when such question is on whether to apply a strict construction or a liberal one on statutes that grant tax exemptions.

12. Because taxes are the lifeblood of the nation, the Court has always applied the doctrine of strict interpretation in construing tax exemptions. Furthermore, a claim of statutory exemption from taxation should be manifest and unmistakable from the language of the law on which it is based. Thus, the claimed exemption 'must expressly be granted in a statute stated in a language too clear to be mistaken.'

13. On the issue of compromise penalties, it has long been held that tax laws imposing penalties for delinquencies are intended to hasten tax payments by punishing evasions or neglect of duty in respect

thereof. If penalties could be condoned for flimsy reasons, the law imposing penalties for delinquencies would be rendered nugatory, and the maintenance of the Government and its multifarious activities will be adversely affected.

14. Further, the Supreme Court has likewise explained that it is mandatory to collect penalty and interest at the stated rate in case of delinquency. The intention of the law is to discourage delay in the payment of taxes due the Government and, in this sense, the penalty and interest are not penal but compensatory for the concomitant use of the funds by the taxpayer beyond the date when he is supposed to have paid them to the Government.

15. Lastly, it has also been held that all presumptions are in favor of the correctness of tax assessment. The good faith of tax assessors and the validity of their actions are presumed. They will be presumed to have taken into consideration all the facts to which their attention was called. It is incumbent upon the taxpayer to prove the contrary and failure to do so shall vest legality to respondent's actions and assessments." *(Citations omitted)*

<u>CTA CASE NO. 7832</u>

"8. Petitioner St. Luke's Medical Center Inc. is liable to pay its deficiency taxes comprising Income Tax, Value-Added Tax, Withholding Tax on Compensation, Expanded Withholding Tax and Documentary Stamp Tax for taxable year 2004 in the total amount of Two Hundred Eighty Seven Million Two Hundred Twenty Two Thousand Two Hundred Fifty Nine and 61/100 (P287,222,259.61) including penalties, surcharges and interest for the following reasons:

8.1 Sec. 27 of the National Internal Revenue Code (NIRC) of 1997 states the following:

'Section 27. Rates on Income Tax on Domestic Corporation.

xxx xxx xxx

(B) *Proprietary Educational Institutions and Hospitals*. – Proprietary educational institutions and **hospitals which are nonprofit shall pay a tax of ten percent (10%) on their taxable income** except those covered by Subsection (D) hereof: *Provided*, that if the gross income from unrelated trade, business or other activity exceeds fifty percent (50%) of the total gross income derived by such educational institutions or hospitals from all sources, the tax prescribed in Subsection (A) hereof shall be imposed on the entire taxable income. For purposes of this Subsection, the term 'unrelated trade, business or other activity' means any trade, business or other activity, the conduct of which is not substantially related to the exercise or performance by such educational institution or hospital of its primary purpose or function. A *'Proprietary educational institution'* is any private school maintained and administered by private individuals or groups with an issued permit to operate from the Department of Education, Culture and Sports (DECS), or the Commission on Higher Education (CHED), or the Technical Education and Skills Development Authority (TESDA), as the case may be, in accordance with existing laws and regulations. (emphasis supplied)

Considering that petitioner is a non-profit hospital, it is subjected to a preferential rate of ten (10%) percent for its income for taxable year 2004.

8.2 Petitioner primarily anchors its argument that it is exempt from the payment of the deficiency taxes on the basis of Section 30(E) and 30(G) of the National Internal Revenue Code of 1997.

Relative to the issue at hand, Section 30 of the NIRC of 1997 reveals:

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

> (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 inures to the benefit of any member, organizer, officer or any specific person; (Emphasis supplied.)
>
> (G) Civic league or organization not organized for profit but operated exclusively for the promotion of social welfare;

The last paragraph of said section likewise provides the following:

> 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.'

The foregoing provision of law is not applicable to the case at hand because said law explicitly provides that the only instance when a non-stock charitable corporation or association may be exempt from the payment of income tax is when said corporation is ***organized and operated exclusively*** for charitable purposes and that ***no part of its income or asset shall belong or inure*** to the benefit of any member, organizer, officer or any specific person. It bears stressing that the law uses the conjunction 'and' instead of using the conjunction 'or' to combine the phrases necessary to entitle a non-stock charitable institution for non-payment of income tax.

First and foremost, the law is explicit and clear, it must be organized and operated ***'exclusively'*** for charitable purposes. The income and assets of petitioner shall be used only for the purpose for which said charitable institution is organized. Neither does the law state that it must be organized and operated 'primarily' for the promotion of the purposes for which it was constituted. Well-settled is the principle that when the law speaks in clear and categorical language, there is no room for interpretation. All that has to be done is to apply the law in every case that falls within its terms. The word 'exclusive' is not a technical term that requires analytical and critical thinking. It is a word that is not difficult to comprehend, so plain to be mistaken and devoid of different interpretations.

In ***G.R. No. 144104 dated June 29, 2004 entitled 'Lung Center of the Philippines vs. Quezon City and Constantino P. Rosas***, the Supreme Court had the occasion to define the word 'exclusive'. It held that:

> **'Exclusive'** is defined as possessed and enjoyed to the exclusion of others; debarred from participation or enjoyment; and 'exclusively' is defined, 'in a manner to exclude; as enjoying a privilege exclusively'. If real property is used for one or more commercial purposes, it is not exclusively used for the exempted purposes but is subject to taxation. The word 'dominant use' or 'principal use' cannot be substituted for the words 'used exclusively' without doing violence to the Constitution and the law. 'Solely' is synonymous with exclusively.'

Petitioner is therefore burdened to prove, by clear and unequivocal proof that it is an institution that is organized and operated ***'exclusively'*** for charitable purposes in order to be entitled to the claim of exemption from the payment of the assessed deficiency taxes for the taxable year 2004.

Petitioner asserts that its Articles of Incorporation reveals that it is a non-stock, non-profit corporation which is established allegedly for the promotion of the charitable and social welfare. Assuming arguendo that said corporation is indeed a non-stock, non-profit corporation, still it is ostensibly a glaring reality that could no longer hide under the cloak of being a charitable institution that said organization is established primarily for the purpose of engaging in business in pursuit of profit and that the performance of charitable and social welfare activities becomes merely a secondary purpose. It is very evident on its operation and conduct of activities that it is **not** operated purely and exclusively for charitable or social welfare purposes.

In ***G.R. No. 144104 dated June 29, 2004 entitled 'Lung Center of the Philippines vs. Quezon City and Constantino P. Rosas***, the Supreme Court held:

> 'To determine whether an enterprise is a charitable institution/entity or not, the elements which should be considered include the statute creating the enterprise, its corporate purpose, its constitution and by-laws, the method of administration, the nature of the actual work performed, the character of the services rendered, the indefiniteness of the beneficiaries, and the use/occupation of the properties; In the legal sense, a charity may be fully defined as a gift, to be applied consistently with existing laws, for the benefit of an indefinite number of persons, either by bringing their minds and hearts under the influence of education or religion, by assisting them to establish themselves in life or otherwise lessening the burden of government. **The test whether an enterprise is charitable or not is whether it is maintained for gain, profit or private advantage**.' **(Emphasis supplied.)**

Verification made on the taxpayer's accounting records show the following information:

> a. Majority of the income is derived from the paying patients who utilizes the medical services offered by petitioner. While we concede that the admission of pay patients does not detract from the charitable character of a hospital. However, it shall hold true only provided that **all of its funds are devoted exclusively to the maintenance of the institution as a 'public charity'.**

In relation thereto, in No. L-15270 dated September 30, 1961 entitled ***'Jose V. Herrera and Esther Herrera vs. Quezon City Board of***

Assessment Appeals', the Supreme Court made the pronouncement that:

> 'The admission of pay patients does not detract from the charitable character of a hospital, if **all of its funds are devoted exclusively to the maintenance of the institution as a 'public charity'**. In other words, 'where rendering charity is its primary object and the funds made by patients able to pay are devoted to the benevolent purposes of the institution, the mere fact that a profit has been made will not deprive the hospital of its benevolent character'

b. **'Free Services'** rendered by petitioner in the amount of P434,056,455.57 represents only a mere 13% of its operations while the remaining 88% represents revenues from services rendered to paying patients. It is noteworthy to say that the alleged 'free services' are mostly availed of by the hospital employees and dependents. A copy of the Detail of Discrepancies relative to the deficiency income tax of petitioner is hereto attached as Annex 'A' and made an integral part hereof'.

c. Income acknowledge by petitioner under the heading **'Non-operating and Other Income'** which is derived from unrelated trade, business and other activity of petitioner, the conduct of which is not substantially related to the exercise or performance by petitioner of its primary purpose or functions amounted to P90,199,463.00. A copy of the Annual Income Tax Return (BIR Form No. 1702) filed by petitioner is hereto attached as Annex 'B' and made an integral part hereof.

d. Donations allegedly made to the Philippine Episcopal Church Diocese for taxable year 2004 amounted only to P7,304,000.00 or a measly .002197 or .2197% of the total Gross Revenues declared in the Annual Income Tax Return (1702) for taxable year 2004.

e. Petitioner does not deny the fact that it likewise derived income from its Pharmaceutical business. Selling of drugs and other pharmacy items to in-patients as well as out-patients does not form part of its hospital services. Dispensing of drugs is different from the selling of drugs.

f. Rental Income is likewise derived on account of the space occupied on the Ground Floor of petitioner's Main Bldg. by Saint's Inc. Coffee Shop, which is represented by YMO Incorporated. A copy of the Contract of Lease entered into between Saint's Inc. Coffee Shop reveals that monthly rental to be paid by said coffee shop is Forty Thousand Pesos (P40,000) or three (3%) percent of the monthly Gross Sales of the lessee, whichever is higher. It likewise stated that the percentage on gross sales is subject to review after two (2) years. A copy of the Contract of Lease as well as the Summary of the Monthly Payments for taxable year 2004 in the amount of One Million Six Hundred Twenty One Thousand Eight Hundred Fifteen and 83/100 (P1,621,815.83) is hereto attached as Annex 'C' and 'D' and made an integral part hereof. Said provision of the contract reveals the business strategy which petitioner employs to earn profit and to have a big slice of the amount of the earnings of the lessee.

g. Petitioner's hospital is situated within a sprawling land area located on E. Rodriguez Sr. Avenue, Quezon City. Within the compound are extension clinics being occupied by physicians who engage in private practice, occupied commercial spaces that cater to the needs of its clients and a banking institution which is likewise strategically located within the premises of petitioner's occupied area. Whether the spaces herein referred to are being rented out to said occupants or offered for free by petitioner in line with the promotion of charitable or social welfare purposes is only within petitioner's knowledge.

h. Respondent would like to invite the attention of this Honorable Court to the Contract of Lease dated August 3, 2001 entered into between Fort Bonifacio Development Corporation herein referred to as the LESSOR and St. Luke's Medical Center, herein referred to as the LESSEE which was pre-marked as Annex "AA" and made an integral part of its Petition for Review. It must be observed that some of the pertinent provisions of the contract include the following:

'WITNESSETH: That

xxx xxx xxx

WHEREAS, the LESSEE intends to lease several parcels of land from the LESSOR, to develop, construct and operate thereon a technically advance medical center comprising mainly of a tertiary hospital, physician offices and other related facilities such as parking structure and **commercial facilities (the 'Structure')** which shall be located in the parcels of land identified as Block 16 xxx' (Emphasis supplied.)

Section 3.5 of the contract provides:

The monthly rental for the portion of the Leased Premises and Structure that are utilized as **commercial and retail spaces** by the Lessee during the Lease Period shall be fixed at twenty percent (20%) of Net Rentals derived by the LESSEE. **The term 'Net Rental' as used in this contract shall mean the total amount of all rent income or rent revenues from all commercial and retail businesses conducted in, upon or from the Leased premises or Structure** xxx (Emphasis supplied.)

Section 3.7 of the contract provides:

Any lease, sublease, sale or disposal in whatsoever manner of spaces in the medical arts building. Physician's offices and parking spaces allotted to medical arts building shall be rated at ten (10%) percent of all collected Net Sales. The term 'Net Sales' as used in this Contract shall mean the total amount of all income or revenues collected by the LESSEE **from the lease, sublease, sale or disposal in whatever manner of any or all spaces in the medical arts building or physicians offices including parking spaces alloted to medical arts building in or upon or from the Leased Premises or Structure, xxx** Net Sales shall not include the amount of value-added tax, sales, excise or

> gross receipts tax imposed...xxx... **on rent collected from customers**. (Emphasis supplied.)

It is crystal clear that the contract reveals the objective of petitioner to engage in business as shown by provisions relating to the establishment of commercial facilities and spaces offered for lease/sublease to prospective tenants and occupants. The establishment is strategically located in the heart of Global City in Fort Bonifacio, considered as one of the best and premiere areas for business growth and development. Suffice it to say that petitioner has only one thing in mind and that is to engage in business to gain profit and private advantage, a far cry from the very purpose which it seeks to establish and create as embodied in its Articles of Incorporation.

8.3 The law explicitly provides that 'that ***no part of its income or asset shall belong or inure*** to the benefit of any member, organizer, officer or any specific person.

The Supreme Court held ***in Lung Center of the Philippines vs. Quezon City and Constantino Rosas,*** that:

> 'As a general principle, a charitable institution does not lose its character as such and its exemption from taxes simply because it derived income from paying patients, whether out-patients or confined in the hospital, or receives subsidies from the government, so long **as the money received is devoted or used altogether to the charitable object which it is intended to achieve; and no money inures to the private benefit of the persons managing or operating the institution.**'

Petitioner's practices as revealed by the investigation points out that the board of trustees, officers and employees of the company stand to directly benefit from the profits and assets of the company. This is a direct contravention of the very provision to where the taxpayer anchors its own argument for exemption. An abstract of the company's ledger which is shown in Final Assessment Notice (FAN) reveal the amount of ₱773,141,824.85 being directly appropriated to its board of trustees, officers and employees. A copy of FAN is hereto attached as Annex 'E' and made an integral part hereof.

The following figures were revealed on account of the investigation:

Salaries and Wages	P554,381,562.54
SSS, Medicare and ECC Premiums	26,342,372.12
Pag-Ibig Premium	2,772,620.27
Honorarium	16,547,526.51
Vacation Leave	16,413,384.85
Sick Leave	14,416,671.21
Meal Allowance	21,062,711.48
Training/Seminar & Staff Development	18,265,444.41
Employee Benefits	23,981,624.90
Performance Bonus	33,936,062.37
Uniform	4,056,171.50
Sports Recreation	1,396,204.60
Provision for Retirement Benefits	39,569,467.79
Total	P773,141,824.85

Of the total company operating expenses of ₱2,663,701,496.14 for 2004, the company spent a hefty 29.02% or ₱773,141,824.85 for remuneration and other benefits to its officers and employees. On top of that are the cost of medical benefits being extended to the same group of people in the form of discounts ranging from 20% - 100% from medical services and medicines. Fringe Benefits are likewise allocated to the Board of Trustees and Officers of petitioner.

8.4 To further bolster its claim and justify its non-payment of income tax, petitioner submitted as part of their documentary evidence a Letter of Exemption dated June 6, 1990 issued by respondent. Said letter recognizes petitioner within the purview of a corporation organized purely for charitable and social welfare purpose and thus, exempt from the payment of income tax and the filing of corresponding income tax return pursuant to Section 26 (e) of the then NIRC of 1986, as amended. (Emphasis supplied.)

Respondent submits that said 1990 Letter of Exemption is no longer valid and subsisting. Hence, no longer applicable to the 2004 deficiency income tax liability of petitioner in view of the amendments introduced by Section 27(B) and 30 (E) of the NIRC of 1997.

In 1990, when the ruling was issued by respondent, non-stock, non-profit hospitals were exempt from payments of income tax by virtue of the express provision of Section 26(e) of the **NIRC of 1986**, the prevailing Tax Code in that particular year. Section 26 (e) of the old Tax Code avers:

> '**Section 26. Exemptions from tax on Corporations.** The following organizations shall not be taxed under this Title in respect to income received by them as such –
>
> xxx xxx xxx
>
> (e) Corporation or association organized and exclusively used for religious, charitable, scientific, athletic, or cultural purposes, or for the rehabilitation of veterans, no part of the net income of which inures to the benefit of any private stockholder or individual.'

Undoubtedly, the law made no distinction relative to the kind of corporations or associations which may avail of the benefits laid down under Section 26(e) of the NIRC of 1986. By express provision, it covers all types of corporation, be it established to gain profit or not or issues stocks or not so long as said corporations are organized and operated ***exclusively*** for the different purposes enumerated therein. In view thereof and armed with a Letter of Exemption from respondent, petitioner enjoyed the benefits of exemption from non-payment of income tax for taxable years 1990 to 1997.

Relative thereto, Section 24(b) of the old Tax Code provides:

> 'Section 24 (b) Private Educational Institution.

> Private Educational Institution, whether stock or non-stock, shall pay a tax of 10% on their taxable income except those covered by Paragraph (e) thereof. xxx'

However, in 1998, Republic Act of 8424 entitled 'National Internal Revenue Code of 1997 was enacted, the Legislature radically changed the provision under Sec 24 (B) of the old Tax Code. Under the NIRC of 1997, particularly Section 27(B) which adopted the provision of Section 24(B) of the old Tax Code, it presently states that aside from Proprietary Educational Institution, **non-profit hospitals** are now likewise required to pay ten (10%) percent of their taxable income, except those subject to final withholding taxes, provided that if the gross income from unrelated trade, business or other activity exceeds fifty (50%) percent of the total gross income by such hospitals from all sources, the rates imposed on subsection (A) thereof shall be imposed on the entire taxable income.

Hence, the legislative intent of Congress to tax hospitals, although operated as non-profit, is very evident and clearly expressed in RA 8424. Crystal clear from the foregoing provision of law is the fact that non-profit hospitals are now liable to pay ten (10%) percent on its taxable income except those covered by Section (D) of the NIRC of 1997. This new provision enacted by the Legislature unmistakably intended to amend the exemption on non-profit hospital that were previously categorized as non-stock, non-profit corporations under Section 26(E) of the 1977 Tax Code. The 1990 ruling being invoked by petitioner is deemed repealed by Section 27(B) of the NIRC of 1997. Consequently, respondent has no other option but to enforce the law on the basis of the defenses herein propounded.

Lastly, Revenue Memorandum Ruling Memo-033-2003 dated September 19, 2003 issued by Milagros V. Regalado (Assistant Commissioner for Legal Service) provides:

> 'The basic difference between Section 27(B) and Section 30(E) is that the former particularly mentions non-profit hospitals, while the latter generally enumerates non-stock corporations organized and operated exclusively, among other things, for charitable purposes. Basic and axiomatic is the rule on statutory construction that the specific provision should always prevail over the general provision.
>
> Section 27(B) does not provide any prohibition in the allocation of its net income as distinguished from Section 30(E), which requires that '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.' Although there is no explicit requirement for non-profit hospital to allot a certain percentage of its net income for charitable purposes, Section 27(B) considers non-profit hospitals as ordinary corporations but subject to a preferential rate of 10%. xxx'

8.5 Another important consideration is the indisputable fact that respondent's filing of his Answer against petitioner signifies as a revocation of the Letter of Exemption dated June 9, 1990 made by respondent, stating that petitioner is exempt from payment of income tax.

In **G.R. No. *153205 dated January 22, 2007 entitled Commissioner of Internal Revenue vs. Burmeister Wain Scandinavian Contractor Mindanao Inc. (BWMSCI)***, the Supreme Court held:

> 'Petitioner's filing of his Answer before the CTA challenging respondent's claim for refund effectively serves as a revocation of VAT Ruling No. 003-99 and BIR Ruling No. 023-95.xxx
>
> However, upon the filing of petitioner's Answer dated March 2, 2000 before the CTA contesting respondent's claim for refund, respondent's services shall be subject to the regular 10% VAT. Such ruling is deemed a revocation of VAT Ruling No. 003-99 and BIR Ruling 23-95.'

The aforementioned case is in relation with the earlier VAT and BIR Rulings issued in favor of BWSCMI insofar as it held that the services being rendered by BMWSCMI is subject to VAT at zero percent (0%). No less than the Honorable Supreme Court has spoken that indeed, the act of filing an Answer before the Court of Tax Appeals by petitioner (Bureau of Internal Revenue) is tantamount to a revocation of the rulings held in favor of the respondent corporation on the basis of Section 108 [previously Section 102] of the NIRC of 1997.

8.7 Having the abovementioned statements as a premise, petitioner should prove by clear and convincing evidence that it is entitled to a claim of exemption from non-payment of deficiency taxes. In relation thereto, Section 16 of the NIRC of 1997 provides:

> '**Section 16. Corporations liable to tax.**
>
> xxx xxx xxx
>
> The tax imposed by law on corporations is not imposed only upon such corporations as are organized and operated for profit. Any corporation, firm or association, no matter how created or organized, or what the purpose of its organization may be, is subject to the tax, except as provided in Section 27, relative to exemptions from tax on corporations. ***A corporation is not exempt simply and only because it is primarily not organized and operated for profit.***' (Emphasis supplied.)

In relation thereto, Section 24 of the Revenue Regulations No. 2, as amended, or otherwise known as Income Tax Regulations provides:

> '**Section 24. Proof Exemption**.
>
> In order to establish its exemption, and thus be relieved of the duty of filing returns of income and paying the tax, it is necessary that every organization claiming exemption **file an affidavit** with the Commissioner of Internal Revenue,

> **showing the character of the organization, the purpose for which it was organized, its actual activities, its source of income and its disposition, whether or not any of its income is credited to surplus or inures or may inure to the benefit of any private shareholder or individual and in general, all facts relating to its operations which affect its right to exemption.** To such affidavit should be attached a copy of the charter or articles of incorporation, the by-laws of the organization and the latest financial statement showing assets, liabilities, receipts and disbursements of the organization.
>
> xxx xxx xxx'

Petitioner utterly failed to prove by clear and categorical evidence that it is still exempted from non-payment of its deficiency income tax. Time and again, respondent avers that tax exemptions must be strictly construed against petitioner and cannot be allowed unless granted in the most explicit and categorical language too plain to be mistaken. They cannot be extended by mere implication or inference. Affirmatively put, the law frowns on exemption from taxation, hence an exemption provision should be construed strictissimi juris. Suffice it to say that it is not enough that a corporation is simply not organized for profit in order to be exempt from the payment of deficiency taxes. Neither is exemption to be presumed from the nature of its establishment, but rather, there should be a categorical provision of law granting the exemption.

As pointed out in the case of ***'Lung Center of the Philippines vs. Quezon City and Constantino P. Rosas***, which is a case that is likewise asserted in the Petition for Review filed by petitioner before this Honorable Court, the Supreme Court cited Section 2 of the Presidential Decree (PD) No. 1823 **explicitly exempting** Lung Center of the Philippines, a non-stock, non-profit hospital from the payment of income tax and gift tax. Section 2 of PD No. 1823 provides:

> 'Section 2. Tax Exemptions and Privileges.

Being a non-profit, non stock corporation organized primarily to help combat the high incidence of lung and pulmonary diseases in the Philippines, all donations, contributions, endowments and equipment and supplies to be imported by authorized entities or persons and by the Board of Trustees of the Lung Center of the Philippines, Inc. for the actual use and benefit of the Lung Center, shall be ***exempt from income and gift taxes***, the same further deductible in full for the purpose of determining the maximum deductible amount under Section 30 Paragraph (h) of the National Internal Revenue Code, as amended. (Emphasis supplied.)

xxx xxx xxx'

Likewise, As held in ***Salvation Army vs. Hochru*** [188 S.W.2d.826 (1945)]:

'An intention on the part of the legislature to grant an exemption from the taxing power of the state will never be implied from language which will admit of any other reasonable construction. Such an intention must be expressed in clear and unmistakable terms, or must appear by necessary implication from the language used, for it is a well settled principle that, when a special privilege or exemption is claimed under a statute, charter or act of incorporation it is to be construed strictly against the property owner and in favor of the public. This principle applies with peculiar force to a claim of exemption from taxation.' (Emphasis supplied.)

8.6 Petitioner's 2004 book of accounts and other accounting records were investigated on account of Letter of Authority No. 00041198 dated February 5, 2007 covering all internal revenue taxes for the period January 1 to December 31, 2004.

Petitioner's claim that the Preliminary Assessment Notice (PAN) was issued without the benefit of Informal Conference is devoid of merit. The Notice of Informal Conference was served to petitioner on November 26, 2007. Petitioner was given 10 days or until December 6, 2007 to refute the assessments against it by respondent. However, the taxpayer's representative did not appear on said date. Such being the case, respondent has no option left but to issue the PAN on account of petitioner's waiver of his right to a preliminary conference. Hence, the claim of petitioner that they were not given opportunity to 'present their side of the case' is without basis. No one should be faulted except petitioner for its failure to exercise its right to be heard. Respondent's issuance of the PAN is therefore valid and within the bounds of law.

8.7 As regards tax deficiencies for Value-Added Tax (VAT), petitioner shall be charged the corresponding VAT on the medicine and pharmaceutical items sold to out-patients, on rental income earned, write-off of long overdue payable to suppliers and proceeds from the sale of property and equipment on the basis of provision on VAT under Section 106 (A) and (B) of the NIRC of 1997.

Likewise, on the basis of the audit/investigation conducted, Expanded Withholding Tax (EWT) shall be charged relative to the variances in income payments made to local suppliers, for contractors and sub-contractors as well as Professional Fees and Honorarium in violation of Section 3 of Revenue Regulations (RR) No. 30-2003 and Section 2.57.2 of RR No. 2-98 in relation to Section 57(B) [Withholding Tax at Source] of the NIRC of 1997.

Similarly, Performance and Christmas Bonus as well as Residents and Intern Salaries were not subjected to proper withholding tax as provided by Section 79 (Income Tax Collected At Source) in relation to Section 24 (Income Tax Rates) of the NIRC of 1997.

Lastly, Contracts executed with Saints, Inc. Coffee Shop and Fort Bonifacio Inc. were not subjected to the corresponding Documentary Stamp Tax pursuant to Section 194 of the NIRC of 1997.

A copy of the FAN detailing the aforementioned Details of Discrepancies is hereto attached and marked as Annex 'E'

8.8 The Supreme Court has likewise explained that it is mandatory to collect penalty and interest at the stated rate in case of delinquency. The intention of the law is to discourage delay in the payment of taxes due the Government and, in this sense, the penalty and interest are not penal but compensatory for the concomitant use of the funds by the taxpayer beyond the date when he is supposed to have paid them to the Government.

8.9 Lastly, it has also been held that all presumptions are in favor of the correctness of tax assessment. The good faith of tax assessors and the validity of their actions are presumed. They will be presumed to have taken into consideration all the facts to which their attention was called. It is incumbent upon the taxpayer to prove the contrary and failure to do so shall vest legality to respondent's actions and assessments."

Upon Motion[11] of petitioner, the Court appointed Mr. Orlan Marigmen as an Independent Certified Public Accountant (CPA) on April 21, 2010.[12]

During trial, petitioner presented Ms. Cristina Hangod, Ms. Ellen R. Gawigawen, Rt. Rev. Manuel C. Lumpias, Mr. Romeo B. Mary, Mr. Orlan H. Marigmen, Dr. Alejandro C. Dizon, Mr. Federico R. Marquez, Jr., and Ms. Amparo M. Faigal as witnesses.

Petitioner filed its Formal Offer of Evidence[13] on November 2, 2011 and its Supplemental Offer of Evidence[14] on November 9, 2012, submitting Exhibits "A" to "Y5-1"; which this Court substantially admitted by way of

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[11] Docket, pp. 406-409.
[12] Minutes, Docket, p. 422.
[13] Docket, pp. 611-634.
[14] Docket, pp. 819-825.

Resolutions dated December 1, 2011, April 17, 2012, December 5, 2012, and January 30, 2013.

The documentary evidence formally offered and admitted are as follows:

Exhibits	Description
A	Audit Results/Assessment Notice No. QA-07-000094 with Assessment Notice Attachment for deficiency income tax for the year 2003
A-1	The amount ₱97,700,084.50
A-2	The date November 22, 2007
B	Audit Results/Assessment Notice No. QA-07-000095 with Assessment Notice Attachment for deficiency income tax for the year 2004
B-1	The amount ₱134,841,854.84
B-2	The date November 22, 2007
C	SLMC's administrative protest dated January 10, 2008
C-1	BIR stamped received on January 14, 2008
D	SLMC's VAT Registration
E	SLMC's Annual Income Tax Return for taxable year 2003
E-1	SLMC's Audited Financial Statements for taxable year 2003
E-3	BIR stamp received on April 13, 2004 by Ms. Maribeth G. Laguntad
F	SLMC's Annual Income Tax Return for taxable year 2004
F-1	SLMC's Audited Financial Statements for taxable year 2004
F-2	SLMC's Statements of Revenues and Expenses for taxable year 2004
F-3	BIR stamped received on April 14, 2005
G	Articles of Incorporation of SLMC
G-1	SLMC's primary purposes
H	BIR Letter of Exemption dated June 6, 1990

H-1	The phrase: "*xxx this Office is of the opinion and so holds that the St. Luke's Medical Center, Inc. falls within the purview of a corporation for purely charitable and social welfare purposes as contemplated under Section 26 (e) & (g) [now Section 30] of the [NIRC] as amended. Accordingly, it is exempt from the payment of income tax on income received by it as such organization, and therefore, need not file an income tax return concerning such income.* xxx "
I	SLMC's BIR/PCNC Certificate of Registration No. 010-2001 dated February 2, 2001
J	SLMC's BIR / PCNC Certificate of Registration No. 062-2006 dated June 28, 2006
K	Certification of SLMC's membership in the National Council of Social Development Foundation of the Philippines, Inc. dated August 15, 2000
L	Certification of SLMC's membership in the National Council of Social Development Foundation of the Philippines, Inc. dated August 24, 2005
M	Certification of SLMC's membership in the National Council of Social Development Foundation of the Philippines, Inc. dated August 10, 2007
N	Department of Social Welfare and Development (DSWD) certification that SLMC, a non-stock, non-profit charitable institution, is its recognized partner
O	Province of Capiz, Roxas City Resolution No. 306, Series of 1999, "Äuthorizing the Honorable Vicente B. Bermejo to enter into a Memorandum of Agreement for a Hospital Twinning Program with St. Luke's Medical Center (SLMC) for and in behalf of the Province of Capiz", adopted on December 3, 1999.
P	Memorandum of Agreement between Roxas Memorial Provincial Hospital and St. Luke's Medical Center dated December 7, 1999.
Q	Mountain Province, Bontoc Sangguniang Panlalawigan Resolution No. 63, Series of 2002, "A Resolution of Recognition and Appreciation to the St. Luke's Medical Center, Quezon City, for its effort to help the hospital in Mountain Province", adopted March 18, 2002
R	Letter from Sister Teresita Montanano, DC of White Cross Children's Home addressed to the Manager of St. Luke's Medical Center dated

	September 25, 2002
S	Letter of appreciation dated January 15, 2002 from Ms. Nelia F. Treseñe of Bahay Pangarap addressed to Mr. Jose Ledesma, President of St. Luke''s Medical Center
U	Memorandum of Agreement between National Children's Hospital and SLMC dated November 18, 1999
V	Memorandum of Agreement between PCSO and SLMC dated July 6, 2001
W	Respondent's Formal Letter of Demand
W-1	SLMC stamp received January 21, 2008
X	Details of Discrepancies
Y	Audit Result/Assessment Notice No. INC-04-000205 for alleged deficiency income tax
Y-1	The amount P237,079,523.66
Z	Audit Result/Assessment Notice No. VT-04-000246 for alleged deficiency value-added tax.
Z-1	The amount P1,116,454.50
AA	Audit Result/Assessment Notice No. WC-04-000105 for alleged deficiency withholding tax on compensation
AA-1	The amount P31,546,727.95
BB	Audit Result/Assessment Notice No. EWT-04-000195 for alleged deficiency expanded withholding tax
BB-1	The amount P17,141,312.74
CC	Audit Result/Assessment Notice No. DST-04-000162 for alleged deficiency documentary stamp tax.
CC-1	The amount P338,695.76
DD	Petitioner's administrative protest dated February 20, 2008 and filed on even date
DD-1	The date February 20, 2008
EE	Respondent's letter dated November 21, 2007
EE-1	The date November 26, 2007 stamped received by SLMC
EE-2	Summary of Results of Investigation

FF	Petitioner's letter to respondent dated December 5, 2007
FF-1	BIR stamped received on December 5, 2007
GG	Preliminary Assessment Notice (PAN)
GG-1	Petitioner SLMC stamped received date on December 19, 2007.
GG-2	Breakdown of Assessment in the PAN
HH	Petitioner's letter to respondent dated December 27, 2007 and received by respondent on even date.
II	Petitioner's reply to the PAN dated January 18, 2008
II-1	Respondent BIR stamped received date on January 21, 2008.
JJ	Report of SLMC's Billing and Accounts Services Department on means employed to collect bad debts that have been written off.
KK	Schedule showing withholding of taxes on Honorarium.
LL	Alpha List of SLMC's Extension Clinic – Professional Fees of Doctors.
LL-1	Alpha List of SLMC's Extension Clinic – Compensation
MM	Alpha List of compensation subject to withholding tax – compensation.
NN	Alpha List of doctors of SLMC's Main Hospital.
OO	SLMC's Alpha List of regular suppliers for 2004.
PP	SLMC's schedule of payments to government entities.
QQ	Certificate of Exemption of the Episcopal Church.
RR	SLMC's DOH License to Operate
SS	Contract of Lease between SLMC and Fort Bonifacio Development Corporation
TT	SLMC's Social Services Department Plaque of Recognition from Province of Pangasinan
UU	Letter of Ms. Cristina S. Hangod dated October 6, 2004 from the Barangay Operations Center, Quezon City
VV	Letter to Mr. Jose Ledesma dated October 7, 2004 from the Office of the Mayor of Quezon City

WW	Judicial Affidavit of Ms. Cristina Hangod dated February 20, 2009.
WW-1	Signature of Ms. Cristina Hangod
YY	Province of Capiz, Roxas City Resolution No. 306, Series of 1999, "Authorizing the Honorable Vicente B. Bermejo to enter in a Memorandum of Agreement for a Hospital Twinning Program with St. Luke's Medical Center (SLMC) for and in behalf of the Province of Capiz", adopted on December 3, 1999
ZZ	Memorandum of Agreement between Roxas Memorial Provincial Hospital and St. Luke's Medical Center dated December 7, 1999
AAA	Mountain Province, Bontoc Sangguniang Panlalawigan Resolution No. 63, Series of 2002, "A Resolution of Recognition and Appreciation to the St. Luke's Medical Center, Quezon City, for its effort to help the hospitals in Mountain Province", adopted March 18, 2002
BBB	Letter of Negros Occidental, Municipality of Cauayan Municipal Mayor Jerry M. Tabujara addressed to Ms. Ellen Gawin-Gawin of St. Luke's Medical Center dated March 31, 2000.
CCC	Letter from the Office of the Provincial Governor, Province of Nueva Vizcaya for medical-dental mission of the Sagip Bayan Foundation and SLMC dated October 23, 2004.
DDD	Certificate of Appreciation (for the delivery of quality health care services, surgical mission) from the Office of the Mayor, Municipality of Cabiao, Province of Nueva Ecija dated October 5, 2004.
EEE	Letter from St. Theodore's Hospital to St. Luke's Medical Center acknowledging receipt of funds for hospital renovations dated February 1, 2002.
FFF	Letter of gratitude dated June 7, 2002 from St. Theodore's Hospital for the donation by St. Luke's Medical Center of an Anesthesia Machine.
GGG	Letter from Fr. Mer and Deisy Karganilla of the Juan Alano Memorial Hospital, Inc., Isabela, Basilan Province addressed to Ms. Ellen Gawigawen of St. Lukes's Medical Center dated March 21, 2001.
HHH	Letter of Appreciation from the Air Force General Hospital dated February 6, 2004 addressed to Ms. Ellen Gawigawen.

III	Certificate of Appreciation dated June 10, 2004 of Lunday Study Center for rendering free medical services to the residents of Parel and Bangan, Botolan, Zambales.
JJJ-2	St. Luke's Medical Center Cash Voucher dated May 27, 2004 for initial donation of P700,000.00 for building the church in Sultan Kudarat.
JJJ-3	BPI Deposit/Payment Slip dated June 3, 2004, depositing the amount of P700,000.00 to the account of Episcopal Diocese of Southern Philippines.
KKK	St. Luke's Medical Center Cash Voucher dated October 25, 2004 for cash donation in the amount of P800,000.00 for construction of a church in Sultan Kudarat.;
KKK-1	BPI Deposit/Payment Slip dated October 28, 2004 depositing the amount of P800,000.00 to the account of Episcopal Diocese of Southern Philippines.
LLL	St. Luke's Medical Center Cash Voucher dated September 7, 2004 for 2nd payment for the construction of the church in Sultan Kudarat.
LLL-1	Equitable PCI Account Information Slip under the name of Episcopal Diocese of Southern Phils. Account No. 1198-04327-10 Makakua Branch-Cotabato City, in the amount of P400,000.00.
MMM	St. Luke's Medical Center Cash Voucher dated November 24, 2004 for payment of additional works on the Isulan church building in Sultan Kudarat in the amount of P619,000.00
MMM-1	BPI Deposit/Payment Slip dated December 8, 2004 depositing the amount of P619,000.00 to the account of Episcopal Diocese of Southern Philippines.
MMM-2	Picture clippings "St. Luke's The Evangelist Church, Isulan Sultan Kudarat Southern Diocese".
NNN	Letter from Ms. Leticia G. Uy of Episcopal Diocese of Southern Phils. Dated October 22, 2004 addressed to Mr. Romeo Mary, Manager, Accounting Department of St. Luke's Medical Center.
OOO	Resolution No. 2 Series of 2004 issued by the Episcopal Diocese of North Central Philippines Holy Innocents Episcopal Church, expressing gratitude to St. Luke's Medical Center of Quezon City for its generous grant in the completion of the on-going

	parish building, dated April 24, 2004.
OOO-1	St. Luke's Medical Center Cash Voucher dated June 22, 2004 for cash donation in the amount of P1,875,000.00.
OOO-2	BPI Deposit/Payment Slip dated June 29, 2004 depositing the amount of P1,875,000.00 to the account of Episcopal Diocese North Central Phils.
PPP	Letter of appreciation dated February 27, 2004 from the Episcopal Diocese of Central Phils. to St. Luke's Medical Center for the donation in the amount of P30,000.00
QQQ	Thank you letter dated December 4, 2003 from the Tagumpay Elementary School to Ms. Ellen Gawigawen, Outreach Program Coordinator of St. Luke's, for school equipment received on November 10, 2003.
RRR	Letter of Appreciation dated July 30, 2003 from La Paz District Hospital to St. Luke's Medical Center thru Ms. Ellen Gawigawen, Outreach Program Coordinator of St. Luke's, for the hospital equipment received.
RRR-1	Thank you letter dated July 30, 2003 from La Paz District Hospital to St. Luke's Medical Center thru Ms. Ellen Gawigawen, Outreach Program Coordinator of St. Luke's, for reusable hospital equipment and apparatus.
SSS	Letter of Appreciation dated June 7, 2003 from J. Cabahug Hospital to Mr. Jose F.G. Ledesma, St. Luke's Medical Center for various hospital equipment received.
TTT	Letter of Appreciation dated May 28, 2003 from Office of the First Lady City of San Jose Del Monte, to Ms. Ellen Gawigawen, Outreach Program Coordinator of St. Luke's Medical Center, for the successful Medical Mission (Operation Tuli) and linen donation to City Health Department.
TTT-1	Letter dated May 27, 2003 to Dr. Arsenio Cantos from the Outreach Program Coordinator re: Operation tuli, San Jose del Monte City, Bulacan.
VVV	Letter of Request dated December 8, 2003 to Ms. Milagros Tolentino, Office of the Gentle, Malacañang from Ms. Ellen R. Gawigawen, Outreach Program Coordinator, St. Luke's Medical Center on donations for the Cataract Operation in Bacolod City.
VVV-1	Pull Out Slip – Inventory Control Section St. Luke's

	Medical Center Sterile Supply re: various Items.
WWW	Letter of Appreciation dated June 23, 2004 from Gen. Vicente Lim Elementary School, Magsaysay Village, Tondo to Ms. Ellen Gawigawen, Outreach Program Coordinator, St. Luke's Medical Center, for school materials and equipment.
XXX	Letter of Appreciation dated July 29, 2004 from the City Social Welfare and Development Department, Mandaluyong City to Mr. Jose Ledesma, Pres. and CEO, St. Luke's Medical Center, for donation of equipment.
YYY	Letter of Appreciation dated May 5, 2004 from the Municipality of Cabiao, Office of the Mayor, Nueva Ecija to Mr. Jose Ledesma, Pres. and CEO, St. Luke's Medical Center, for donation of medical equipment.
YYY-1	Letter of Solicitation from the Office of the Mayor, Cabiao, Nueva Ecija date May 6, 2004.
ZZZ	Letter to Ms. Ellen Gawigawen dated March 5, 2004 from Bethlemhem House of Bread, Little Baguio, Baliuag.
AAAA	Kapasiyahan dated Enero 27, 2003 issued by the Office of the Barangay, Sta. Maria, Bayan ng Mansalay.
BBBB	Letter to Jose Ledesma dated December 31, 2004 from the Office of the Sangguniang Bayan, Municipality of Victoria, Laguna.
CCCC	Letter to Jose Ledesma date September 16, 2004 from the Blue Mantle's Temporary Shelter to the Abandoned, Inc.
CCCC-1	Letter to Jose Ledesma dated August 24, 2004 from the Blue Mantle's Temporary Shelter to the Abandoned, Inc.
CCCC-2	Pictures of elderly with their caregivers from the Mantle's Temporary Shelter.
DDDD	Letter of Donation to the Office of the City Health Officer, San Jose Del Monte, Bulacan dated May 8, 2003.
FFFF	SLMC Cash Voucher dated June 21, 2004 of cash donation to Episcopal Diocese of the Northern Phils. Inc. in the amount of P1,280,000.00
FFFF-1	BPI Deposit/Payment Slip dated June 29, 2004 in the amount of P1,280,000.00 to the account of Episcopal Diocese of the Northern Phils.

GGGG	SLMC Cash Voucher dated January 6, 2004 for cash donation to Episcopal Diocese of the Central Phils. Inc. in the amount of P1,000,000.00.
GGGG-1	Official Receipt No. 0169 dated January 9, 2004 issued by the Episcopal Diocese of the Central Phils. to SLMC
HHHH	SLMC Cash Voucher dated December 23, 2003 for cash donation to Episcopal Diocese of Central Phils. Inc. in the amount of P1,000,000.00.
IIII	Judicial Affidavit of Ms. Ellen R. Gawigawen dated March 27, 2009.
IIII-1	Signature of Ms. Ellen R. Gawigawen.
J4	Judicial Affidavit of Rt. Rev. Manuel C. Lumpias dated May 29, 2009.
J4-1	Signature of Rt. Rev. Manuel C. Lumpias.
K4	CTA Decision dated February 23, 2009 in CTA Case No. 6746.
L4	CTA Decision dated November 21, 2008 in CTA Case No. 6993.
M4	Schedule/Statement of Revenues and Expenses for 2003 and 2004 prepared by Mr. Romeo B. Mary.
N4	Judicial Affidavit of Mr. Romeo B. Mary dated October 15, 2009.
N4-1	Signature of Mr. Romeo B. Mary.
O4	Other Income/Expense Schedule
O4-1	Schedule of Investments in Trust Funds; Financial Reports, Supporting Investing Schedules
O4-2, O4-2-1 to 273	Photocopies of relevant documents supporting schedule of Investments in Trust Funds
P4	Schedule of Bad Debts Expense
P4-1	General Policy of Writing-off worthless or uncollectible accounts (Billing and Accounts Service Department)
Q4	Schedule of Professional Fees – H.O. for taxable period 2004
Q4-1	Alphalist of EWT – Professional Fees – H.O.
R4	Schedule of Honorarium
S4	Schedule of VAT-Corp. Registered Supplier of

	Goods
S4-1 **S4-1-1 to S4-1-233** **S4-1-235 to S4-1-414** **S4-1-416 to S4-1-520** **S4-1-525 to S4-1-697**	Photocopies of relevant documents e.g., official receipts, invoices supporting schedule of VAT-Corp. Registered Supplier of Goods
S4-2	Schedule of Verified VAT-Corp. Registered Supplier of Goods
T4	Schedule of VAT-Corp. Contractor
T4-1	Schedule of verified VAT-Corp. Contractor
T4-2 **T4-2-1 to 174**	Photocopies of relevant documents e.g., official receipts, invoices supporting schedule of VAT-Corp. Contractor
U4	Schedule of VAT-Individual Contractor
U4-1	Schedule of verified VAT-Individual Contractor
U4-2 **U4-2-1 to 71**	Photocopies of relevant documents e.g., official receipts, invoices supporting schedule of VAT-Individual Contractor
V4	Schedule of VAT-Registered Individual Supplier of Goods
V4-1	Schedule of verified VAT-Registered Individual Supplier of Goods
V4-2 **V4-2-1 to 203**	Photocopies of relevant documents e.g., official receipts, invoices supporting Schedule of VAT-Registered Individual Supplier of Goods
W4	Schedule of VAT-Corp. Registered Supplier of Services
W4-1	Schedule of verified VAT-Corp. Registered Supplier of Services
W4-2 **W4-2-1**	Photocopies of relevant documents e.g., official receipts, invoices supporting Schedule of VAT-Corp. Registered Supplier of Services
X4	Schedule of Donations to Episcopal Churches
X4-1	Schedule of verified Donations to Episcopal Churches
X4-2 **X4-2-1 to 26**	Photocopies of relevant documents e.g., official receipts, invoices in support of Schedule of Donations to Episcopal Churches

Y4	Schedule of payment to Quezon City Government & Laguna Lake Development Authority (LLDA)
Y4-1 **Y4-1-1 to 14**	Photocopies of relevant documents e.g., official receipts, invoices in support of Schedule of payment to Quezon City Government & Laguna Lake Development Authority (LLDA)
Z4	Schedule of Exempt Transaction for Imported Medical Equipments, Instruments, Medical Supplies, Research Supplies and Replacement Supplies
Z4-1 **Z4-1-1 to 174** **Z4-1-176 to 181** **Z4-1-183 to 536**	Photocopies of relevant documents e.g., official receipts, invoices in support of Schedule of Exempt Transaction for Imported Medical Equipments, Instruments, Medical Supplies, Research Supplies and Replacement Supplies
A5	Schedule of VAT (CPIP/ Advertising/ Recruitment/ Research – 15%)
A5-1 **A5-1-1 to 2**	Photocopies of relevant documents e.g., official receipts, invoices supporting Schedule of VAT (CPIP/ Advertising/ Recruitment/ Research – 15%)
B5	Schedule of VAT (CPIP/ Advertising/ Recruitment/ Research – 10%)
B5-1 **B5-1-1** **B5-1-3**	Photocopies of relevant documents e.g., official receipts, invoices supporting Schedule of VAT (CPIP/ Advertising/ Recruitment/ Research – 10%)
C5	Schedule of Interns Account for taxable year 2004
D5	Schedule of Resident Doctors Account for taxable year 2004
D5-1	Payroll Disbursement Register
E5	Vouchers and relevant documents supporting Christmas Bonus
E5-1-1 to 22	Photocopies of Vouchers & relevant documents supporting Christmas Bonuses
F5	Schedule of Performance Bonus-Extension Clinic
F5-1	Photocopies of relevant documents e.g., official receipts, invoices supporting Schedule of Performance Bonus
G5	Certificates of accreditation from different recognized medical societies
H5	Report prepared by duly-commissioned

	Independent Certified Public Accountant (ICPA), Mr. Orlan H. Marigmen
H5-1	Signature of Mr. Orlan H. Marigmen
I5	Judicial Affidavit of Mr. Orlan H. Marigmen
I5-1	Signature of Mr. Orlan H. Marigmen
IIIII	Letter of Dr. Arsenio C. Cantos M.D. dated 10 January 2001 to Dr. Alejandro Dizon, M.D. approving his appointment as Chief Training Officer of St. Luke's Medical Center
JJJJJ	Letter of Dr. Arsenio C. Cantos, M.D. and Mr. Jose F.G. Ledesma, President and Chief Executive Officer to Dr. Alejandro Dizon, M.D. dated 18 December 2003, approving his appointment as Assistant Medical Director for Graduate Medical Education and Training Officer of St. Luke's Medical Center
KKKKK	Job Description of Chief Training Officer implemented on September 2003
KKKKK-1	Page Two (2) of Job Description of Chief Training Officer
KKKKK-2	Page Three (3) of Job Description of Chief Training Officer
KKKKK-3	Page Four (4) of Job Description of Chief Training Officer
KKKKK-4	Page Five (5) of Job Description of Chief Training Officer
LLLLL	Job Description of Resident implemented on October 2002
LLLLL-1	Page Two (2) of Job Description of Resident
LLLLL-2	Page Three (3) of Job Description of Resident
LLLLL-3	Page Four (4) of Job Description of Resident
LLLLL-4	Page Five (5) of Job Description of Resident
LLLLL-5	Page Six (6) of Job Description of Resident
LLLLL-6	Page Seven (7) of Job Description of Resident
LLLLL-6-A	Printed name of Alejandro Dizon, M.D.
LLLLL-6-B	Signature of Alejandro Dizon, M.D.
MMMMM	St. Luke's Medical Center Graduate Medical Education Table of Organization of Medical Affairs Division dated March 2004

NNNNN	St. Luke's Medical Center Collective Bargaining Agreement 2000-2005
NNNNN-1	The text of the CBA which reads: "It is understood that resident physicians, fellow and interns are not employees of the HOSPITAL and are not covered by this agreement"
PPPPP	Judicial Affidavit of Dr. Alejandro C. Dizon
PPPPP-1	Signature of Dr. Alejandro Dizon
SSSSS	Job Description of Vice President implemented on May 2008
SSSSS-1	Name and signature of Mr. Federico Marquez
T5	Judicial Affidavit of Mr. Federico R. Marquez, Jr. executed on March 21, 2011
W5	Judicial Affidavit of Ms. Amparo M. Faigal executed on June 28, 2011
W5-1	Signature of Ms. Amparo M. Faigal
X5	Supplemental Report dated August 23, 2012, prepared by the duly-commissioned Independent Certified Public Accountant (ICPA), Mr. Orlan H. Marigmen
X5-1	Signature of Mr. Orlan H. Marigmen
Y5	Judicial Affidavit of Mr. Orlan H. Marigmen executed on August 23, 2012
Y5-1	Signature of Mr. Orlan H. Marigmen

On the other hand, respondent filed her Formal Offer of Evidence[15] on May 25, 2012, submitting Exhibits "1" to "14-A", inclusive of sub-markings; which this Court admitted by way of Resolution dated July 13, 2012.

Respondent's documentary evidence are as follows:

Exhibit	Description
1	Letter of Authority No. LOA 00041198 dated 5 February 2007.
2	Notice of Informal Conference dated 21 November 2007.

[15] Docket, pp. 714-722.

2-A	Name and signature of Mr. Romulo L. Aguila, Jr.
2-B	Stamp receipt of St. Luke's Medical Center, Inc. and the name Oyet Ninon.
3	Preliminary Assessment Notice.
3-A	Name and signature of Mr. Romulo L. Aguila, Jr.
3-B	Stamp receipt of St. Luke's Medical Center, Inc.
3-C	Details of Discrepancies.
4	Formal Letter of Demand with Details of Discrepancies.
4-A	Name and signature of Mr. Romulo L. Aguila, Jr.
4-B	Name and signature of Mr. Romeo B. Mary.
4-C	Details of Discrepancies.
5	Audit Results/Assessment Notice for deficiency Documentary Stamp Tax (DST).
6	Audit Results/Assessment Notice for deficiency Withholding Tax on Compensation.
7	Audit Results/Assessment Notice for deficiency Expanded Withholding Tax (EWT).
8	Audit Results/Assessment Notice for deficiency Value-Added Tax (VAT).
9	Audit Results/Assessment Notice for deficiency Income Tax.
10	Memorandum Report dated 7 December 2007.
10-A	Name and signature of Rogelio P. Gonzales.
11	Judicial Affidavit of Rogelio P. Gonzales.
11-A	Name and signature of Rogelio P. Gonzales.
12	First Request for Presentation of Records/Documents dated 5 February 2007.
12-A	Name and signature of Rogelio P. Gonzales.
13	Second Request for Presentation of Records/Documents dated 16 February 2007.

13-A	Name and signature of Rogelio P. Gonzales.
14	Final Request for Presentation of Records/Documents dated 17 April 2007.
14-A	Name and signature of Rogelio P. Gonzales.

In the Resolution dated March 8, 2013, the instant case was submitted for decision, taking into consideration respondent's Memorandum filed on December 26, 2012 and petitioner's Memorandum filed on March 4, 2013.

The parties submitted the following issues[16] for this Court's resolution:

"1. Whether Respondent's right to assess Petitioner for alleged deficiency income tax for the taxable year 2003 is already barred by the statute of limitations.

2. Whether Petitioner is a non-stock, non-profit corporation organized for charitable and social welfare purposes under Section 30(E) and (G) of the NIRC or a non-profit hospital under Section 27(B) of the 1997 NIRC.

3. Whether or not the Letter of Exemption dated June 6, 1990 issued by Respondent to Petitioner, which forms part of the documentary evidence submitted by Petitioner, where it exempts the latter from payment of income tax and filing of corresponding income tax return is still valid and subsisting and therefore, applicable to the deficiency income tax liability of Petitioner.

4. Whether or not Petitioner is liable to pay the assessment for the taxable year 2004 in the

[16] Docket, pp. 216-217.

total deficiency tax of Two Hundred Eighty-Seven Million Two Hundred Twenty-Two Thousand Two Hundred Fifty-Nine Pesos and 61/100 (₱287,222,259.61) comprising deficiency income tax in the amount of ₱237,079,523.66, deficiency value-added tax amounting to ₱1,116,454.49, deficiency withholding tax on compensation amounting to ₱31,546,727.95, deficiency expanded withholding tax amounting to ₱17,141,312.72 and deficiency documentary stamp tax in the amount of ₱338,695.76, including penalties, surcharges and interest.

5. Whether Respondent erred in disallowing certain expenses from Petitioner's 2004 net income.

6. Whether Petitioner failed to withhold taxes on certain income payments subject to expanded withholding tax.

7. Whether Petitioner is liable for compromise penalties for alleged non-compliance with Section 248(A) of the NIRC, as amended by Republic Act No. 8424.

The Court shall resolve first the issue of prescription with respect to the deficiency income tax.

Periods of limitation upon the assessment of taxes

The period within which internal revenue taxes may be assessed and collected is laid down in Sections 203 and 222 of the NIRC of 1997, as amended, to wit:

"SEC. 203. *Period of Limitation Upon Assessment and Collection.* - Except as provided in Section 222,

> internal revenue taxes shall be assessed within three (3) years after the last day prescribed by law for the filing of the return, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period: *Provided*, That in a case where a return is filed beyond the period prescribed by law, the three (3)-year period shall be counted from the day the return was filed. For purposes of this Section, a return filed before the last day prescribed by law for the filing thereof shall be considered as filed on such last day."

Based on Section 203, internal revenue taxes must be assessed within three (3) years counted from the last day of the period fixed by law for the filing of the tax return or the actual date of filing, whichever is later. This rule governs matters relating to prescription of the government's right to assess internal revenue taxes primarily to safeguard the interests of taxpayers from unreasonable investigation.

Necessarily therefore, the government must assess internal revenue taxes on time so as not to extend indefinitely the period of assessment and deprive the taxpayer of the assurance that it will no longer be subjected to further investigation for taxes after the expiration of a reasonable period of time.[17]

However, it must be pointed out that the three-year prescriptive period for the BIR to assess tax liabilities under Section 203 of the NIRC of 1997 is applicable to returns that are regularly filed pursuant to legal requirements.

But when the government is placed at a disadvantage so as to prevent its lawful agents from proper assessment of tax liabilities due to a false return, fraudulent return intended to evade payment of tax or failure to file returns, the prescriptive period is ten (10) years after the discovery of the falsity, fraud or omission. In the absence of a false or fraudulent return with intent to evade tax, and where a

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[17] *Commissioner of Internal Revenue vs. FMF Development Corporation*, G.R. No. 167765, June 30, 2008.

return has been filed, the period of limitation may be extended, where the taxpayer and the Commissioner have agreed in writing to its assessment prior to the expiration of the time prescribed in Section 203 for the assessment of the tax, and after such time, the tax may still be assessed within the period agreed upon. These scenarios are governed by Section 222 of the NIRC of 1997, to wit:

> "SEC. 222. *Exceptions as to Period of Limitation of Assessment and Collection of Taxes*. –
>
> (a) In the case of a false or fraudulent return with intent to evade tax or of failure to file a return, the tax may be assessed, or a proceeding in court for the collection of such tax may be filed without assessment, at any time within ten (10) years after the discovery of the falsity, fraud or omission: *Provided*, That in a fraud assessment which has become final and executory, the fact of fraud shall be judicially taken cognizance of in the civil or criminal action for the collection thereof.
>
> (b) If before the expiration of the time prescribed in Section 203 for the assessment of the tax, both the Commissioner and the taxpayer have agreed in writing to its assessment after such time, the tax may be assessed within the period agreed upon. The period so agreed upon may be extended by subsequent written agreement made before the expiration of the period previously agreed upon.
>
> (c) Any internal revenue tax which has been assessed within the period of limitation as prescribed in paragraph (a) hereof may be collected by distraint or levy or by a proceeding in court within five (5) years following the assessment of the tax.
>
> (d) Any internal revenue tax, which has been assessed within the period agreed upon as provided in paragraph (b) hereinabove, may be collected by distraint or levy or by a proceeding in court within the period agreed upon in writing before the expiration of the five (5)-year period. The period so agreed upon may be extended by subsequent written agreements

> made before the expiration of the period previously agreed upon.
>
> (e) *Provided, however*, That nothing in the immediately preceding Section and paragraph (a) hereof shall be construed to authorize the examination and investigation or inquiry into any tax return filed in accordance with the provisions of any tax amnesty law or decree."

Clearly, the three-year period to assess is applicable to petitioner considering that none of the exceptions stated in Section 222 is applicable to petitioner; thus, the 3-year period to assess petitioner for its deficiency income tax for the taxable year 2003 commences from the date after the last day prescribed by law for the filing of the return, which is the 15th day of the fourth month following the close of the taxpayer's taxable year.

As may be gleaned from the records of the case, petitioner employs the calendar year as basis for filing its Annual Income Tax Return. Petitioner filed its Annual Income Tax Return for the taxable year 2003 on April 13, 2004. Counting from April 15, 2004, respondent had until April 15, 2007 to assess petitioner for its deficiency income tax for the taxable year 2003. However, respondent issued Audit Results/Assessment Notice No. QA-07-000094 for deficiency income tax for the year 2003 against petitioner only on November 22, 2007, which is way beyond the 3-year period prescribed by law. Hence, petitioner's assessment for deficiency income tax for the taxable year 2003 should be cancelled and withdrawn for having been issued beyond the 3-year prescriptive period provided by law.

A. DEFICIENCY EXPANDED WITHHOLDING TAX - ₱17,141,312.73

In the Formal Letter of Demand, respondent found petitioner liable for deficiency EWT on professional fees, honorarium and various income payments for the taxable year 2004 in the amount of ₱17,141,312.73, computed as follows:

	Professional Fees (Extension Clinic)	Professional Fees/ Honorarium (Main Hospital)	Various Income payments	Total
Basic Deficiency EWT	₱ 183,263.07	₱ 2,902,590.04	₱ 7,620,744.90	₱ 10,706,598.01
Add: Interest (1/11/05 to 12/31/07)	109,012.24	1,726,577.19	4,533,125.29	6,368,714.72
Penalties	16,000.00	25,000.00	25,000.00	66,000.00
Total amount due and collectible	**₱308,275.30**	**₱4,654,167.23**	**₱12,178,870.19**	**₱17,141,312.73**

1. Payments for professional fees and honorarium

According to respondent, professional fees and honorarium were not properly subjected to EWT of 10% if the amount of income payment does not exceed ₱720,000.00 and 15% in excess thereof, in violation of Section 3 of Revenue Regulations (RR) No. 30-03 and Section 2.57.2 of RR No. 02-98 in relation to Section 57(B) of the NIRC of 1997, as amended, resulting in a deficiency EWT of ₱308,275.30 and ₱4,654,167.23, inclusive of interest and compromise penalties, the detailed computations of which are shown below:

PROFESSIONAL FEES IN EXCESS OF ₱720K (EXTENSION CLINIC)								
Payee	Amount	₱720K	Excess of ₱720K	Tax Due in Excess of ₱720K	Tax Due on ₱720K	Total Tax Due	Tax Paid	Still Due
Asis, Redentor	2,012,221.80	720,000.00	1,292,221.80	193,833.27	72,000.00	265,833.27	201,222.18	64,611.09
Sy, Jerry	1,009,160.70	720,000.00	289,160.70	43,374.11	72,000.00	115,374.11	100,916.07	14,458.04
Mendoza, Merlene	966,952.00	720,000.00	246,952.00	37,042.80	72,000.00	109,042.80	96,695.20	12,347.60
Cantos, Arsenio	957,754.80	720,000.00	237,754.80	35,663.22	72,000.00	107,663.22	95,775.48	11,887.74
Lorenzo, Juliet	957,754.80	720,000.00	237,754.80	35,663.22	72,000.00	107,663.22	95,775.48	11,887.74
Marchadesch, Leticia	892,881.80	720,000.00	172,881.80	25,932.27	72,000.00	97,932.27	89,288.18	8,644.09
Milo, Mario	892,128.00	720,000.00	172,128.00	25,819.20	72,000.00	97,819.20	89,212.80	8,606.40
Tingcungco, Angelito	892,128.00	720,000.00	172,128.00	25,819.20	72,000.00	97,819.20	89,212.80	8,606.40

Mejia, Manuel, Jr.	891,639.90	720,000.00	171,639.90	25,745.99	72,000.00	97,745.99	89,163.99	8,582.00
Gapasin, Judith	876,111.90	720,000.00	156,111.90	23,416.79	72,000.00	95,416.79	87,611.19	7,805.60
Cerezo, Freman	860,119.20	720,000.00	140,119.20	21,017.88	72,000.00	93,017.88	86,011.92	7,005.96
Tucay, Agnes	822,838.00	720,000.00	102,838.00	15,425.70	72,000.00	87,425.70	82,283.80	5,141.90
Zantua, Raphael Ryan	806,941.60	720,000.00	86,941.60	13,041.24	72,000.00	85,041.24	80,694.16	4,347.08
Tiu, Dionisio	798,661.10	720,000.00	78,661.10	11,799.17	72,000.00	83,799.17	79,866.11	3,933.05
Griño, Lilibeth	794,922.40	720,000.00	74,922.40	11,238.36	72,000.00	83,238.36	79,492.24	3,746.12
Payumo, Ronald Alan	753,045.30	720,000.00	33,045.30	4,956.80	72,000.00	76,956.80	75,304.53	1,652.27
Discrepancy			**3,665,261.30**			**1,701,789.20**	**1,518,526.13**	**183,263.07**
Interest								109,012.24
Compromise								16,000.00
Total								**308,275.31**

PROFESSIONAL FEES IN EXCESS OF ₱720K (MAIN HOSPITAL)								
Payee	**Amount**	**₱720K**	**Excess of ₱720K**	**Tax Due in Excess of ₱720K**	**Tax Due on ₱720K**	**Total Tax Due**	**Tax Paid**	**Still Due**
Bondoc, Edgardo	1,597,969.37	720,000.00	877,969.37	131,695.41	72,000.00	203,695.41	202,378.80	1,316.61
Calleja, Homobono	1,884,093.83	720,000.00	1,164,093.83	174,614.07	72,000.00	246,614.07	239,172.81	7,441.26
Cervantes, Julieta	1,272,032.67	720,000.00	552,032.67	82,804.90	72,000.00	154,804.90	151,414.51	3,390.39
Cuanang, Joven	1,702,800.70	720,000.00	982,800.70	147,420.11	72,000.00	219,420.11	179,245.00	40,175.10
De Castro, Estanislao	3,848,845.03	720,000.00	3,128,845.03	469,326.75	72,000.00	541,326.75	514,233.64	27,093.11
Dy, Pilar	2,989,345.20	720,000.00	2,269,345.20	340,401.78	72,000.00	412,401.78	410,978.94	1,422.84
Eduardo, Emmanuel	2,227,042.90	720,000.00	1,507,042.90	226,056.44	72,000.00	298,056.44	286,264.55	11,791.89
Estrera, Dahlia Virgina	2,294,127.27	720,000.00	1,574,127.27	236,119.09	72,000.00	308,119.09	300,828.55	7,290.54
Joson, Rafael	7,058,124.47	720,000.00	6,338,124.47	950,718.67	72,000.00	1,022,718.67	981,526.58	41,192.09
Kuizon, Danilo A	1,868,541.03	720,000.00	1,148,541.03	172,281.15	72,000.00	244,281.15	240,484.21	3,796.94
Lazatin, Benedict M	2,508,234.20	720,000.00	1,788,234.20	268,235.13	72,000.00	340,235.13	336,461.34	3,773.79
Lazo, Henry	8,212,900.17	720,000.00	7,492,900.17	1,123,935.03	72,000.00	1,195,935.03	1,127,709.53	68,225.50
Lo, Raymundo W	5,372,726.30	720,000.00	4,652,726.30	697,908.95	72,000.00	769,908.95	735,446.00	34,462.94
Lopez, Rolando	3,780,462.73	720,000.00	3,060,462.73	459,069.41	72,000.00	531,069.41	515,384.57	15,684.84
Miranda, Ariel	3,526,225.73	720,000.00	2,806,225.73	420,933.86	72,000.00	492,933.86	481,047.43	11,886.43
Narciso, Francisco	4,769,782.17	720,000.00	4,049,782.17	607,467.33	72,000.00	679,467.33	653,039.11	26,428.22
Ramos, Roberto	7,118,230.00	720,000.00	6,398,230.00	959,734.50	72,000.00	1,031,734.50	989,202.41	42,532.09
Reyes, Augusto	1,051,835.20	720,000.00	331,835.20	49,775.28	72,000.00	121,775.28	108,476.00	13,299.28
Rogelio, Gregorio	2,714,432.80	720,000.00	1,994,432.80	299,164.92	72,000.00	371,164.92	369,529.37	1,635.55
Santiago, Jonas	2,456,371.47	720,000.00	1,736,371.47	260,455.72	72,000.00	332,455.72	330,175.51	2,280.21
Serrano, Vivian	1,475,031.63	720,000.00	755,031.63	113,254.74	72,000.00	185,254.74	183,321.04	1,933.70
SP Castro, Associates	1,200,000.00	720,000.00	480,000.00	72,000.00	72,000.00	144,000.00	120,000.00	24,000.00
Yunque, Abondino	980,770.87	720,000.00	260,770.87	39,115.63	72,000.00	111,115.63	98,167.84	12,947.79
Zamuco, Jaime	1,773,127.63	720,000.00	1,053,127.63	157,969.14	72,000.00	229,969.14	213,509.21	16,459.93
Discrepancy			**56,403,053.37**			**10,188,458.01**	**9,767,996.95**	**420,461.06**

Honorarium not subjected to withholding tax (BIR Ruling 43-2001 & RMC 72-2004)	**16,547,526.51**	**15%**	**2,482,128.98**
Total			**2,902,590.04**
Interest			**1,726,577.19**
Compromise			**25,000.00**
Total			**4,654,167.23**

On the other hand, petitioner contends that professional fees and honorarium were recorded as part of payment to "doctors' professional fees". The corresponding taxes were properly withheld and reported in the alphalist for doctors in compliance with Section 57 of the NIRC of 1997, as amended, and Section 2.57.2 of Revenue Regulations No. 02-98. Petitioner also points out that per its records, honorarium amounted only to ₱11,707,512.49 and not ₱16,547,256.51 as alleged by respondent. Honoraria were given to petitioner's doctors who were appointed as medical heads of various institutes or centers of petitioner. These payments were subjected to withholding tax on professional fees at the rate of either 10% or 15%.

Section 2.57.2 of RR No. 2-98, as amended by RR No. 30-03, provides as follows:

> "(I) *Professional fees paid to medical practitioners.* - Any amount collected for and paid to medical practitioners (includes doctors of medicine, doctors of veterinary science and dentists) by hospitals and clinics, or paid directly to the medical practitioners by patients who were 'admitted and confined' to such Hospitals or Clinics, or paid directly to such medical practitioners by health maintenance organizations (HMOs) and/or similar establishments which is likewise covered by Section 2.57.2(A)(1) - *Fifteen percent (15%), if the income payments to the medical practitioner for the current year exceeds P720,000; and Ten percent (10%), if otherwise."*

Clearly, from the foregoing, income payments to medical practitioners are subject to EWT either at ten percent (10%), if the current year's income payment is ₱720,000.00 and below, or fifteen percent (15%) if the current year's income payment exceeds ₱720,000.00.

A scrutiny of the alphalist attached to the Annual Information Return of Creditable Income Taxes Withheld (Expanded)/Income Payments Exempt from Withholding Tax (BIR Form No. 1604-E)[18] filed by petitioner for its Main Hospital as well as the alphalist of petitioner's Extension Clinic[19] and petitioner's Monthly Remittance Returns of Creditable Income Taxes Withheld(Expanded) (BIR Form No. 1601-E)[20] for the taxable year 2004 show that petitioner used the rate of 10% instead of 15% for some doctors' professional fees exceeding ₱720,000.00 resulting in underwithholding of 5%. This fact was admitted by petitioner in its Memorandum[21].

Respondent, however, erroneously computed the deficiency EWT assessment by applying 10% on ₱720,000.00 and 15% on the excess thereof. Thus, petitioner's deficiency EWT on professional fees paid to doctors for the taxable year 2004 shall be recomputed as follows:

PROFESSIONAL FEES IN EXCESS OF ₱720K (EXTENSION CLINIC)					
Payee	**Income Payments**	**Tax Rate for Income Payments exceeding ₱720,000.00**	**Tax Due**	**Tax Paid**	**Tax Still Due**
Asis, Redentor	₱ 2,012,221.80	15%	₱ 301,833.27	₱ 201,222.18	₱ 100,611.09
Sy, Jerry	1,009,160.70	15%	151,374.11	100,916.07	50,458.04
Mendoza, Merlene	966,952.00	15%	145,042.80	96,695.20	48,347.60
Cantos, Arsenio	957,754.80	15%	143,663.22	95,775.48	47,887.74
Lorenzo, Juliet	957,754.80	15%	143,663.22	95,775.48	47,887.74
Marchadesch, Leticia	892,881.80	15%	133,932.27	89,288.18	44,644.09
Milo, Mario	892,128.00	15%	133,819.20	89,212.80	44,606.40
Tingcungco, Angelito	892,128.00	15%	133,819.20	89,212.80	44,606.40
Mejia, Jr., Manuel	891,639.90	15%	133,745.99	89,163.99	44,582.00
Gapasin, Judith	876,111.90	15%	131,416.79	87,611.19	43,805.60
Cerezo, Freman	860,119.20	15%	129,017.88	86,011.92	43,005.96
Tucay, Agnes	822,838.00	15%	123,425.70	82,283.80	41,141.90
Zantua, Raphael Ryan	806,941.60	15%	121,041.24	80,694.16	40,347.08

[18] Exhibit "NN".
[19] Exhibit "LL".
[20] BIR Records, pp. 183-194.
[21] Petitioner's Memorandum, p. 35.

Tiu, Dionisio	798,661.10	15%	119,799.17	79,866.11	39,933.06
Griño, Lilibeth	794,922.40	15%	119,238.36	79,492.24	39,746.12
Payumo, Ronald Alan	753,045.30	15%	112,956.80	75,304.53	37,652.27
Total	**₱15,185,261.30**		**₱2,277,789.20**	**₱1,518,526.13**	**₱ 759,263.07**

PROFESSIONAL FEES IN EXCESS OF ₱720K (MAIN HOSPITAL)					
Payee	**Income Payments**	**Tax Rate for Income Payments exceeding ₱720,000.00**	**Tax Due**	**Tax Paid**	**Tax Still Due**
Bondoc, Edgardo	₱ 1,597,969.37	15%	₱ 239,695.41	₱ 202,378.80	₱ 37,316.61
Calleja, Homobono	1,884,093.83	15%	282,614.07	239,172.81	43,441.26
Cervantes, Julieta	1,272,032.67	15%	190,804.90	151,414.51	39,390.39
Cuanang, Joven	1,702,800.70	15%	255,420.11	179,245.00	76,175.11
De Castro, Estanislao	3,848,845.03	15%	577,326.75	514,233.64	63,093.11
Dy, Pilar	2,989,345.20	15%	448,401.78	410,978.94	37,422.84
Eduardo, Emmanuel	2,227,042.90	15%	334,056.44	286,264.55	47,791.89
Estrera, Dahlia Virgina	2,294,127.27	15%	344,119.09	300,828.55	43,290.54
Joson, Rafael	7,058,124.47	15%	1,058,718.67	981,526.58	77,192.09
Kuizon, Danilo	1,868,541.03	15%	280,281.15	240,484.21	39,796.94
Lazatin, Benedict	2,508,234.20	15%	376,235.13	336,461.34	39,773.79
Lazo, Henry	8,212,900.17	15%	1,231,935.03	1,127,709.53	104,225.50
Lo, Raymundo	5,372,726.30	15%	805,908.95	735,446.00	70,462.94
Lopez, Rolando	3,780,462.73	15%	567,069.41	515,384.57	51,684.84
Miranda, Ariel	3,526,225.73	15%	528,933.86	481,047.43	47,886.43
Narciso, Francisco	4,769,782.17	15%	715,467.33	653,039.11	62,428.22
Ramos, Roberto	7,118,230.00	15%	1,067,734.50	989,202.41	78,532.09
Reyes, Augusto	1,051,835.20	15%	157,775.28	108,476.00	49,299.28
Rogelio, Gregorio	2,714,432.80	15%	407,164.92	369,529.37	37,635.55
Santiago, Jonas	2,456,371.47	15%	368,455.72	330,175.51	38,280.21
Serrano, Vivian	1,475,031.63	15%	221,254.74	183,321.04	37,933.70
SP Castro, Associates	1,200,000.00	15%	180,000.00	120,000.00	60,000.00
Yunque, Abondino	980,770.87	15%	147,115.63	98,167.84	48,947.79
Zamuco, Jaime	1,773,127.63	15%	265,969.14	213,509.21	52,459.93
Total	**₱73,683,053.37**		**₱11,052,458.01**	**₱9,767,996.95**	**₱1,284,461.06**

Consequently, petitioner shall be liable to pay basic deficiency EWT on doctors' professional fees in the amount of ₱2,043,724.13, computed as follows:

	Basic Deficiency EWT

Professional Fees - Extension Clinic	₱ 1,284,461.06
Professional Fees - Main Hospital	759,263.07
Total	**₱ 2,043,724.13**

As regards the honorarium of ₱16,547,526.51 on which a 15% deficiency EWT was imposed by respondent, petitioner avers that the honorarium that was given to the doctors who were appointed as medical heads of its various institutes or centers amounted only to ₱11,707,512.49 as indicated in the Schedule of Honorarium for the year 2004[22]. However, an examination of the records, particularly petitioner's Trial Balance[23] for the year 2004, shows that petitioner's total honorarium expenses amounted to ₱16,547,256.51 which comprised of the honorarium expenses of the Head Office (₱11,707,512.49) and the Extension Clinic (₱4,840,014.02).

Out of the ₱11,707,512.49 honorarium expense reflected per petitioner's schedule, only the following income payments totalling ₱696,000.00 were traced to petitioner's alphalist for the year 2004[24]:

Payee	**Amount per EWT Alphalist**	**Income Payments Subjected to 10% (WI 151)**	**EWT**	**Income Payments Subjected to 10% (WC 151)**	**EWT**	**Honorarium**
Yasuhiro, Oba	120,000.00	120,000.00	12,000.00	-	-	₱ 120,000.00
Payee	**Amount per EWT Alphalist**	**Income Payments Subjected to 10% (WI 151)**	**EWT**	**Income Payments Subjected to 15% (WI 150)**	**EWT**	**Honorarium**
Bargaza, Nina Gloriani	180,000.00	90,000.00	9,000.00	90,000.00	13,500.00	180,000.00
Garcia, Arnold	138,000.00	69,000.00	6,900.00	69,000.00	10,350.00	138,000.00
Rosario, Annie	138,000.00	69,000.00	6,900.00	69,000.00	10,350.00	138,000.00
Sioson, Virgilio	120,000.00	60,000.00	6,000.00	60,000.00	9,000.00	120,000.00
Total						**₱696,000.00**

[22] Exhibit "R4".
[23] BIR Records, pp. 399-404.
[24] Attached to Exhibit "NN".

Thus, out of petitioner's total honorarium expense for the year 2004 in the amount of ₱16,547,526.51, only the amount of ₱696,000.00 was verified to have been subjected to EWT. As a result, petitioner shall be liable for basic deficiency EWT in the amount of ₱2,377,728.98 on the remaining honorarium expense of ₱15,851,526.51, pursuant to Section 2.57.2(A) of RR No. 2-98, as amended by RR No. 30-2003, computed as follows:

Total Honorarium Expense for the year 2004	₱ 16,547,526.51
Less: Amount verified to have been subjected to EWT	696,000.00
Net Honorarium Expense	₱ 15,851,526.51
EWT Rate	15%
Basic Deficiency EWT on Honorarium Expense for the year 2004	**₱2,377,728.98**

2. Various income payments

Per comparison of petitioner's expense items/income payments as reflected in its financial statements and income tax return with those shown in its alphalist for the year 2004, respondent found that there were income payments to local suppliers of goods, contractors/subcontractors and rent expense in the respective amounts of ₱501,834,595.16, ₱109,310,955.91 and ₱8,323,596.67 which were not subjected to the corresponding 1%, 2% and 5% EWT. Invoking Section 57(B) of the NIRC of 1997, as amended, in relation to Section 2.57.2 of RR No. 2-98, respondent assessed petitioner of basic deficiency EWT of ₱7,620,744.90, computed as follows:

	Expense per F/S	**Amt. subject to 1%**	**Amt. subject to 2%**	**Amt. subject to 5%**
COST OF SERVICES TO PATIENTS				
Medicines and Supplies	₱1,071,166,672.00	₱1,071,166,672.00		
Utilities	121,330,160.00		₱121,330,160.00	
Repairs and Maintenance	106,273,425.00		106,273,425.00	
Office and Housekeeping Supplies	40,731,431.00		40,731,431.00	
Research and Development	22,063,010.00	22,063,010.00		
Outside and Contractual Services	14,147,791.00		14,147,791.00	
Insurance	4,967,918.00		4,967,918.00	

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Professional Services	4,046,738.00			
Legal and Audit Fees (CSP others)	150.00			
Rental (CSP others)	353,808.50			353,808.50
Rental to ECP in the guise of Discount & Donation	8,085,073.57			8,085,073.57
Insurance (CSP others)	434,171.71		434,171.71	
Miscellaneous Expense (CSP others)	3,360,506.46	3,360,506.46		
Marketing and Public Relations (CSP others)	3,666,914.70		3,666,914.70	
ADDITION TO PROPERTY AND EQUIPMENT				
Building and Building Improvement	20,269,135.00	20,269,135.00		
Hospital and Medical Equipment	352,507,312.00	352,507,312.00		
Transportation Equipment	2,372,000.00	2,372,000.00		
Furniture, Fixture Equipment	9,880,988.00	9,880,988.00		
Construction in Progress	130,200,808.00	130,200,808.00		
GENERAL AND ADMINISTRATIVE EXPENSE				
Corporate Affairs				
210501 Advertising & Promotion	16,112,926.00		16,112,926.00	
210503 Corporate Affairs	5,755,911.00		5,755,911.00	
210504 Fund Development	1,884,701.00		1,884,701.00	
Utilities				
210401 Telephone & Telegraph	5,627,164.00		5,627,164.00	
210401 Light, Gas & Water	1,596,299.00		1,596,299.00	
210401 Gasoline & Oil	127,464.00	127,464.00		
Repairs and Maintenance	2,069,510.00		2,069,510.00	
Office Supplies	4,937,622.00	4,937,622.00		
Security Service	9,669,066.00		9,669,066.00	
Janitorial Service	309,211.00		309,211.00	
Outside Service	3,372,876.00		3,372,876.00	
Insurance	4,568,729.00		4,568,729.00	
Legal & Audit Fees	1,673,824.00			
Rental	117,023.00			117,023.00
Property & Furnishing	14,260,143.00	14,260,143.00		
Anniversary	3,710,956.00	3,710,956.00		
Miscellaneous Expense	13,981,981.00	13,981,981.00		
Housekeeping Supplies	559,622.00	559,622.00		
Total	2,006,193,040.94	1,649,398,219.46	342,518,204.41	8,555,905.07
Less: Amount subjected per EWT Alphalist	1,655,039,629.62	1,147,563,624.30	233,207,248.50	232,308.40
Discrepancy	351,153,411.32	501,834,595.16	109,310,955.91	8,323,596.67
Deficiency EWT	**₱ 7,620,744.90**	**₱ 5,018,345.95**	**₱ 2,186,219.12**	**₱416,179.83**

Petitioner contends that respondent, in computing the above deficiency EWT, erroneously included the VAT portion on certain income payments to its regular suppliers, payments to government entities, donations to the

Philippine Episcopal Diocese, purchases of imported equipment, casual purchases, expenses subjected to EWT rate of 10% or 15%, and capitalized lease. After deducting these items, petitioner points out that its liability would be reduced to ₱504,689.72, ₱1,810,615.17 and ₱10,764.61 representing 1%, 2% and 5% basic deficiency EWT, respectively, totalling ₱2,326,069.50, computed as follows:

	Amount subject to 1%	Amount subject to 2%	Amount subject to 5%
Amt. subject to Expanded Withholding Tax per Assessment	₱1,649,398,219.46	₱ 342,518,204.41	₱ 8,555,905.07
Less: Amt. subjected per EWT Alpha List	1,147,563,624.30	233,207,248.50	232,308.40
Add: Amt. not subject of EWT per Petitioner's Protest			
1. VAT on Rent	-	-	23,230.84
2. VAT on Corp. suppliers of goods	98,014,997.00	-	-
3. VAT on Corp. contractors	-	12,029,407.60	-
4. VAT on registered individual contractors	-	1,627,891.00	-
5. VAT on registered individual – Reg. supplier – goods	8,033,311.43	-	-
6. VAT on registered corp. – Reg. suppliers	-	655,981.30	-
7. Donations to Episcopal church for construction of Churches	-	-	8,085,073.57
8. Payment to Laguna Lake Development Authority	1,021,999.98	-	-
9. Payment to QC Government	5,218,831.10	-	-
10. Custom duties, VAT, and import charges on importation of medical equipment	12,462,746.53	-	-
11. VAT on Local Govt. tax and doc stamps on insurance	-	1,167,093.50	-
12. Expenses subjected to 15% or 10% w/tax			
Professional Fee - 15%	3,260,926.24	-	-
Professional Fee - 10% (CIP/advertising/recruitment/research)	10,728,140.28	-	-
13. Exempt transactions - imported medical equipment	171,440,433.09	-	-
14. Imported medical supplies	6,713,951.86	-	-
15. Imported medical replacement parts	-	2,117,938.73	-
16. Imported research supplies	40,919.81	-	-
17. Imported subscription	3,071.66	-	-
18. Imported medical instruments	3,032,344.02	-	-
19. Casual purchases below ₱10,000	1,193,142.14	1,181,885.09	-
20. Construction in Progress (capitalized lease) 2004 is covered by rent free period	130,200,808.00	-	-
Total	₱1,598,929,247.44	₱ 251,987,445.72	₱ 8,340,612.81
Discrepancies	50,468,972.02	90,530,758.69	215,292.26
Deficiency Expanded Withholding Tax	**₱ 504,689.72**	**₱ 1,810,615.17**	**₱ 10,764.61**

The Court will now determine whether or not the foregoing items should be excluded in computing petitioner's deficiency 1%, 2% and 5% EWT for the taxable year 2004.

1. VAT on certain income payments to regular suppliers (Item Nos. 1 to 6)

Petitioner alleges that respondent failed to recognize the fact that in recording its expense and assets, corresponding input VAT were recorded as part of its expenses and/or assets. Petitioner argues that while it is VAT-registered, its activities subject to VAT are limited only to pharmacy sales to out-patients. Petitioner further contends that a VAT-registered person who is also engaged in transactions not subject to VAT is allowed tax credit equivalent to the total input tax which can be directly attributed to transactions subject to value-added-tax.

Moreover, petitioner explains that it incurs expenses for supplies that are used in connection with the medical services rendered by its hospital. Petitioner's regular suppliers are VAT-registered taxpayers and pass on the VAT to petitioner. Since petitioner cannot recognize input VAT arising from these purchases, it adds on as part of costs and records the costs of supplies as the total amount paid to its regular suppliers.

In support, petitioner cites the basic principle in income taxation that taxes are withheld only on income. If an amount constitutes both income and taxes, that portion which corresponds to taxes is not subject to withholding tax.

To prove that the expenses or income payments, subject of the deficiency EWT assessment, are inclusive of VAT, petitioner presented its Schedule of VAT on Rent[25], Schedule of VAT on Corporate Registered Suppliers of Goods[26], Schedule of VAT on Corporate Contractor[27],

[25] Attached to Exhibit "NN".
[26] Exhibit "S4".
[27] Exhibit "T4".

Schedule of VAT on Individual Contractor[28], Schedule of VAT on Individual Registered Suppliers of Goods[29] and Schedule of VAT on Corporate Registered Suppliers of Services[30] and the related cash vouchers, invoices, statements of account, and official receipts. However, the Court finds these documents insufficient. Even though VAT may have been paid or incurred by petitioner on some of its purchases, petitioner failed to clearly establish under what expense or asset accounts such purchases were booked. Petitioner should have presented its detailed general ledger showing all the purchase transactions recorded (inclusive of VAT) under each expense or asset account, subject of the deficiency EWT assessment and reconciled the recorded purchases with those reflected in the VAT schedules and supporting invoices/official receipts. Thus, while the VAT is not subject to withholding tax, petitioner failed to prove that the VAT was included in the income payments upon which the subject deficiency EWT assessment was based.

2. Payments to government entities (Item Nos. 8, 9 and 11)

Petitioner argues that payments such as documentary stamp tax, local government tax and VAT are not among those enumerated as payments subject to withholding tax. Likewise, petitioner avers that penalties paid to Laguna Lake Development Authority (LLDA) and the Quezon City Government, which were booked as "Miscellaneous" are not subject to withholding tax.

Petitioner presented its Schedule of Payment to Government and LLDA[31] for the year 2004, which reflected the following payments to LLDA and Quezon City Treasurer:

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[28] Exhibit "U4".
[29] Exhibit "V4".
[30] Exhibit "W4".
[31] Exhibit "Y4".

Doc. Date	Document No.	Payee	Amount
1/31/2004	3200002122	Laguna Lake Development Authority	₱ 170,333.33
2/9/2004	3200005385	Laguna Lake Development Authority	170,333.33
3/5/2004	3200001167	Laguna Lake Development Authority	170,333.33
4/16/2004	3200001168	Laguna Lake Development Authority	170,333.33
5/7/2004	3200004373	Laguna Lake Development Authority	170,333.33
6/4/2004	3200006724	Laguna Lake Development Authority	170,333.33
Total			**₱1,021,999.98**
5/24/2004	3200005934	Quezon City Treasurer	₱ 18,831.10
7/15/2004	3200008453	Quezon City Treasurer	5,000,000.00
11/4/2004	3200013625	Quezon City Treasurer	200,000.00
Total			**₱5,218,831.10**

However, only the amount of ₱1,021,999.98, representing payment to LLDA of accumulated daily penalties for petitioner's water pollution case, is duly supported by official receipts, statements of account and cash vouchers[32]. Be that as it may, it cannot be ascertained whether the amount of ₱1,021,999.98 formed part of the "Miscellaneous Expense (CSP others)" in the amount of ₱3,360,506.46 (under Cost of Services to Patients) and "Miscellaneous Expense" in the amount of ₱13,981,981.00 (under General and Administrative Expenses), which were subjected by respondent to deficiency 1% EWT. Petitioner should have presented the detailed composition of these Miscellaneous Expense accounts whereby it can be traced that the penalties of ₱1,021,999.98 were included therein.

3. Purchases of imported equipment and casual purchases (Item Nos. 10 and 13 to 19)

Petitioner contends that its purchases of imported equipment, including the payment of the corresponding VAT and customs duties thereon and booked under "Hospital and Medical Equipment" are not subject to withholding tax. Likewise, casual purchases below ₱10,000.00, which were booked under "various expenses", are exempt from the

[32] Exhibits "Y4-1-1" to "Y4-1-14".

withholding tax system under BIR Revenue Regulations No. 17-2003.

Petitioner did not submit documents to substantiate its alleged casual purchases below ₱10,000.00. As regards its importations, petitioner presented its Schedules[33] of Dollar Purchases and Brokerage Fee and Handling for the year 2004 and the related invoices and official receipts[34]. While these documents proved that petitioner actually imported medical equipment and supplies and paid the related customs fees, duties and VAT, however, it cannot be verified whether the same formed part of the account "Hospital and Medical Equipment" in the amount of ₱352,507,312.00 on which a 1% EWT was imposed by respondent. Petitioner should have provided a detailed breakdown of the transactions recorded under the account "Hospital and Medical Equipment". Even though the 1% EWT applies only to local purchases, petitioner failed to show that the importations and customs fees, duties and VAT were included by respondent in the computation of the deficiency 1% EWT assessment.

4. Expenses subjected to 15% or 10% Withholding Tax (Item No. 12)

Per its recomputation of the deficiency 1% expanded withholding tax, petitioner indicated that there were professional fees in the amounts of ₱3,260,926.24 and ₱10,728,140.28 under the accounts of "CIP/ advertising/recruitment/research", which were already subjected to 10% or 15% EWT; thus, were deducted from the total income payments subjected to 1% EWT.

Petitioner submitted its Schedule of VAT (CPIP/Advertising/Recruitment/Research-15[35] and Schedule

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[33] Exhibit "Z[4]"
[34] Exhibit "Z[4]-1"
[35] Exhibit "A[5]".

of VAT (CPIP/Advertising/Recruitment/Research-10%) [36], which reflected the following:

SCHEDULE OF VAT (CPIP/Advertising/Recruitment/Research-15%)					
Supplier Name	**Gross Income**	**Net of VAT**	**Input VAT**	**EWT Rate**	**Tax**
Meinhardt Philippines, Inc.	₱ 1,668,126.24	₱ 1,516,478.40	₱ 151,647.84	15%	₱ 227,471.76
SP Castro and Associates	880,000.00	800,000.00	80,000.00	15%	120,000.00
GAIA South, Inc.	52,800.00	48,000.00	4,800.00	15%	7,200.00
RMLC Design Ventures	660,000.00	600,000.00	60,000.00	15%	90,000.00
Total	**₱3,260,926.24**	**₱2,964,478.40**	**₱296,447.84**		**₱444,671.76**

SCHEDULE OF VAT (CPIP/Advertising/Recruitment/Research-10%)					
Supplier Name	**Gross Income**	**Net of VAT**	**Input VAT**	**EWT Rate**	**Tax**
GAIA South, Inc.	₱ 243,199.99	₱ 221,090.90	₱ 22,109.09	10%	₱ 22,109.09
Imelda Silayan and Partners	467,100.04	424,636.40	42,463.64	10%	42,463.64
Meinhardt Philippines, Inc.	1,725,263.98	1,568,421.80	156,842.18	10%	156,842.18
RMLC Design Ventures	2,640,000.00	2,400,000.00	240,000.00	10%	240,000.00
BIZnews Financial Gazette	33,999.90	30,909.00	3,090.90	10%	3,090.90
Baseline Software Services	160,416.63	145,833.30	14,583.33	10%	14,583.33
Gagni Hipolito	50,000.06	45,454.60	4,545.46	10%	4,545.46
Hire, Inc.	115,830.00	105,300.00	10,530.00	10%	10,530.00
SMDI Consultants, Inc.	312,999.94	284,545.40	28,454.54	10%	28,454.54
WL Segovia and Associates, Inc.	1,265,000.00	1,150,000.00	115,000.00	10%	115,000.00
SP Castro and Associates	2,274,250.00	2,067,500.00	206,750.00	10%	206,750.00
Mannasoft Technology Corp.	37,000.04	33,636.40	3,363.64	10%	3,363.64
Aromin Sy and Associates	189,999.70	172,727.00	17,272.70	10%	17,272.70
ZMG Signum Ward Howell, Inc.	437,580.00	397,800.00	39,780.00	10%	39,780.00
Benedicto Limjap Gavino, Jr.	319,000.00	290,000.00	29,000.00	10%	29,000.00
He Dimanlig Lanscape	280,500.00	255,000.00	25,500.00	10%	25,500.00
Marsh Philippines, Inc.	176,000.00	160,000.00	16,000.00	10%	16,000.00
Total	**₱10,728,140.28**	**₱9,752,854.80**	**₱ 975,285.48**		**₱975,285.48**

A perusal of the alphalist attached to petitioner's Annual Information Return of Creditable Income Taxes Withheld (Expanded)/Income Payments Exempt from Withholding Tax (BIR Form No. 1604-E) [37] shows that petitioner indeed subjected the foregoing professional fees to EWT rate of 10% or 15%. Nevertheless, it cannot be ascertained whether the said professional fees formed part of the amounts subjected by respondent to 1% EWT in the

[36] Exhibit "B[5]".
[37] Exhibit "NN".

absence of the detailed general ledger of the expense or asset accounts under which such professional fees were booked.

5. Construction in Progress (Item No. 20)

A review of petitioner's 2004 Audited Financial Statements (AFS)[38], particularly the Statements of Assets, Liabilities and Fund Balances, shows that petitioner's "Property and Equipment" account includes additions to "Construction In Progress and Others" in the amount of ₱130,200,808.00[39].

As stated in Note 17[40] of the AFS, petitioner entered into a lease agreement with Fort Bonifacio Development Corporation on August 3, 2001 covering several parcels of land where another hospital will be constructed. The lease shall be effective for a period of 50 years renewable for another 25 years from the expiration date.

As part of the agreement, petitioner is entitled to a rent-free period for the first five (5) calendar years and the minimum lease payment of not less than ₱150,000.00 per month after the lessee has not generated revenue after the rent-free period. When the lessee has generated revenues after the rent-free period of 5 years then the rental shall be 2% of net revenues[41].

The AFS shows that the amount of ₱130,200,808.00 pertains to petitioner's capitalized lease payments which are not subject to EWT.

[38] Attached to Exhibit "F-1".
[39] Notes to Financial Statements, under "8. Property and Equipment", attached to Exhibit "F-1".
[40] Notes to Financial Statements, attached to Exhibit "F-1".
[41] Exhibit "Y-5", p. 45.

6. Donations to the Philippine Episcopal Church Diocese (Item No. 7)

Respondent imposed 5% EWT on the amount of ₱8,085,073.57 as "Rental to ECP in the guise of Discount and Donation".

Petitioner, on the other hand, claims that its donations to the Philippine Episcopal Church Diocese for the taxable year 2004 amounting to ₱7,304,000.00 and booked under "Donations" were used for the construction of churches and chapels in the far-flung areas of the Philippines. Petitioner further states that the Philippine Episcopal Church is a duly registered religious corporation that enjoys exemption from both income tax and donor's tax. And as such, said donations are not subject to any withholding tax.

Records show that petitioner indeed made donations to the Philippine Episcopal Church Diocese in the amount of ₱6,674,000.00 as evidenced by the various documents it submitted before this Court, to wit:

Exhibit	Particulars	Amount
"JJJ"	Letter from Episcopal Diocese of Southern Philippines dated June 9, 2004 acknowledging receipt of ₱700,000.00 for construction of church building in Isulan, Sultan Kudarat	
"JJJ-1"	Episcopal Church Official Receipt No. 15915 receiving the amount of ₱700,000.00	
"JJJ-2"	St. Lukes Medical Center Cash Voucher dated May 27, 2004 for initial donation of ₱700,000.00 for building the church in Sultan Kudarat.	
"JJJ-3"	BPI Deposit/Payment Slip dated June 3, 2004 depositing the amount of ₱700,000.00.	₱ 700,000.00
"KKK"	St. Lukes Medical Center Cash Voucher dated October 25, 2004 for cash donation of ₱800,000.00 for construction of a church in Sultan Kudarat.	
"KKK-1"	BPI Deposit/Payment Slip dated October 28, 2004 depositing the amount of ₱800,000.00.	800,000.00
"LLL"	St. Lukes Medical Center Cash Voucher dated September 7, 2004 for second payment for construction of a church in Sultan Kudarat in the amount of ₱400,000.00	400,000.00
"LLL-1"	Equitable PCI Account Information Slip under the name of Episcopal Diocese of Southern Phils. in the amount of ₱400,000.00.	

"NNN"	Letter from Episcopal Diocese of Southern Philippines dated October 22, 2004 acknowledging receipt of ₱400,000.00.	
"NNN-1"	Episcopal Church Official Receipt No. 16122 receiving the amount of ₱400,000.00	
"MMM"	St. Lukes Medical Center Cash Voucher dated November 24, 2004 for payment of additional works on Isulan church building in Sultan Kudarat in the amount ₱619,000.00	
"MMM-1"	BPI Deposit/ Payment Slip dated December 8, 2004 depositing the amount of ₱619,000.00	
"MMM-2"	Picture Clippings of "St. Luke's The Evangelist Church	619,000.00
"OOO"	Resolution expressing gratitude to St. Lukes - North Central Philippines Holy Innocents Episcopal Church	
"OOO-1"	St. Lukes Medical Center CV in the amount of ₱1,875,000.00	
"OOO-2"	BPI Deposit/Payment Slip dated June 29, 2004 depositing the amount of ₱1,875,000.00	1,875,000.00
"FFFF"	SLMC Cash Voucher dated June 21, 2004 for cash donation to Episcopal Diocese of Northern Phils., Inc. in the amount of ₱1,280,000.00	
"FFFF-1"	BPI Deposit/Payment Slip dated June 29, 2004 in the amount of ₱1,280,00000.	1,280,000.00
"GGGG"	SLMC Cash Voucher dated January 6, 2004 for cash donation to Episcopal Diocese of Central Phils., Inc. in the amount of ₱1,000,000.00	
"GGGG-1"	Official Receipt No. 0169 dated January 9, 2004 in the amount of ₱1,000,000.00	1,000,000.00
	Total	**₱6,674,000.00**

Considering that donations are not among those enumerated transactions subject to EWT under RR No. 02-98, the amount of ₱6,674,000.00 should be excluded in computing petitioner's deficiency 5% EWT for the taxable year 2004. However, for petitioner's failure to refute respondent's finding on the rental of ₱1,411,073.57 (₱8,085,073.57 less ₱6,674,000.00), the imposition of 5% EWT thereon shall remain. Consequently, petitioner is liable for basic deficiency 1%, 2% and 5% EWT in the amount ₱5,985,036.82, computed as follows:

	Amount subject to 1%	**Amount subject to 2%**	**Amount subject to 5%**
Amt. subject to Expanded Withholding Tax per Assessment	1,649,398,219.46	342,518,204.41	8,555,905.07
Less: Amt. subjected per EWT Alpha List	1,147,563,624.30	233,207,248.50	232,308.40
Add: Amt. not subject of EWT per Petitioner's Protest			
Donations to Episcopal Church for construction of churches			6,674,000.00
Construction in Progress (capitalized lease) 2004 is covered by rent free period	130,200,808.00		
Total	1,277,764,432.30	233,207,248.50	6,906,308.40
Discrepancies	371,633,787.16	109,310,955.91	1,649,596.67
Deficiency Expanded Withholding Tax	**3,716,337.87**	**2,186,219.12**	**82,479.83**

Total Deficiency Expanded Withholding Tax	**5,985,036.82**

To recapitulate, petitioner's basic deficiency EWT liability on professional fees, honorarium and various income payments for the taxable year 2004 amounts to ₱10,406,489.93, broken down as follows:

Professional Fees - Head Office	₱ 759,263.07
Professional Fees - Extension Office	1,284,461.06
Honorarium	2,377,728.98
Various Income Payments	5,985,036.82
Basic Deficiency EWT	**₱10,406,489.93**

B. DEFICIENCY WITHHOLDING TAX ON COMPENSATION - ₱31,546,272.95

Respondent's investigation disclosed that Performance and Christmas Bonus amounting to ₱39,941,312.37 and Salaries of Residents and Interns amounting to ₱21,822,856.25 were not subjected to proper withholding tax on compensation as provided by Section 79 in relation to Section 24 of the NIRC of 1997, as amended. Consequently, respondent assessed petitioner for deficiency WTC in the amount of ₱31,546,272.95, inclusive of interest and compromise penalty, computed as follows:

Performance and Christmas bonus (RR 2-98 Sec. 2.281(3)11)	₱ 39,941,312.37	32%	₱ 12,781,219.96
Residents and Interns (no withholding tax)	21,822,856.25	32%	6,983,314.00
Basic	₱ 61,764,168.62		₱ 19,764,533.96
Interest from (1/11/05 to 12/31/07)			11,756,738.99
Compromise			25,000.00
Total amount due and collectible			**₱31,546,272.95**

1. Performance and Christmas Bonus

As verified by the Independent CPA, the total amount of ₱39,941,312.37 Performance and Christmas Bonuses given by petitioner for the year 2004 was subjected to tax as follows[42]:

Performance Bonus (Extension Clinic)	
Paid to Doctors subjected to EWT on Professional Fees (PF)-Extension Clinic	₱ 27,499,946.90
Salaries paid to employees subjected to WTC	6,436,115.47
Christmas Bonus (Main Hospital)	
Paid to Employees subjected to WTC	6,005,250.00
Total	**₱ 39,941,312.37**

An examination of petitioner's alphalist for its Extension Clinic shows that petitioner actually withheld and remitted the amount of ₱2,749,994.69 representing 10% EWT on the Perfomance Bonus paid to doctors for the year 2004 in the amount of ₱27,499,946.90. However, there were Performance Bonuses exceeding ₱720,000.00, which pursuant to Section 2.57.2 of RR No. 2-98, as amended by RR No. 30-03, a 15% EWT should have been withheld and remitted. Thus, petitioner shall be liable for basic deficiency EWT in the amount of ₱759,263.06, as computed hereinbelow:

Family Name	First Name	Income Payments	Tax Rate for Income Payments exceeding ₱720,000.00	Tax Due	Tax Paid	Tax Still Due
Asis	Redentor	2,012,221.80	15%	301,833.27	201,222.18	100,611.09
Cantos	Arsenio	957,754.80	15%	143,663.22	95,775.48	47,887.74
Cerezo	Freman	860,119.20	15%	129,017.88	86,011.92	43,005.96
Gapasin	Judith	876,111.90	15%	131,416.79	87,611.19	43,805.60
Grino	Lilibeth	794,922.40	15%	119,238.36	79,492.24	39,746.12
Lorenzo	Juliet	957,754.80	15%	143,663.22	95,775.48	47,887.74
Marchadesch	Leticia	892,881.80	15%	133,932.27	89,288.18	44,644.09
Mejia	Manuel Jr.	891,639.90	15%	133,745.99	89,163.99	44,582.00
Mendoza	Merlene	966,952.00	15%	145,042.80	96,695.20	48,347.60
Milo	Mario	892,128.00	15%	133,819.20	89,212.80	44,606.40
Payumo	Ronald Allan	753,045.30	15%	112,956.80	75,304.53	

[42] Exhibit "Y-5", under "IV. WITHHOLDING TAX ON COMPENSATION", a.(2), p. 39.

						37,652.27
Sy	Jerry	1,009,160.70	15%	151,374.11	100,916.07	50,458.04
Tingcungco	Angelito	892,128.00	15%	133,819.20	89,212.80	44,606.40
Tiu	Dionisio	798,661.10	15%	119,799.17	79,866.11	39,933.06
Tucay	Agnes	822,838.00	15%	123,425.70	82,283.80	41,141.90
Zantua	Raphael Ryan	806,941.60	15%	121,041.24	80,694.16	40,347.08
Total		**15,185,261.30**		**2,277,789.20**	**1,518,526.13**	**759,263.06**

Anent the Performance Bonus paid to employees in the amount of ₱6,436,115.47, the Independent CPA reported that his verification would show that the amount of ₱6,436,115.47 was declared as part of the alphalist of petitioner on compensation – extension clinic under the column of "Taxable 13th Month and Other Benefits".[43] However, petitioner did not submit a schedule listing down the name of each employee, amount of Performance Bonus received and detailed breakdown of the total 13th Month Pay and Other Benefits received by each employee in order for this Court to verify with petitioner's alphalist[44], the actual withholding and remittance of taxes pertaining to the Performance Bonus of ₱6,436,115.47.

As to the Christmas Bonus of ₱6,005,250.00, the Independent CPA reported that his verification of petitioner's schedule of Christmas Bonus and check voucher[45] and alphalist of tax withheld on compensation would show that Christmas Bonuses amounting to ₱4,000.00 per employee were already subjected to withholding tax on compensation as part of "Non-Taxable 13th Month and Other Benefits" if the total does not exceed ₱30,000.00 per employee[46]. Even though the names of the employees listed in the schedule of Christmas Bonus can be traced to the alphalist, it cannot be determined whether the Christmas Bonus formed part of the employee's "Non-Taxable 13th Month and Other Benefits" reflected in the alphalist. Petitioner should have provided a

[43] Exhibit "Y-5", under "IV. WITHHOLDING TAX ON COMPENSATION", a.(3), par. 2, p. 39.
[44] Exhibit "LL-1".
[45] Exhibits "E^5", "E^5-1-1" to "E^5-1-22".
[46] Exhibit "Y-5", under "IV. WITHHOLDING TAX ON COMPENSATION", a.(4), p. 39.
[46] Exhibit "LL-1".

schedule detailing the 13th month, Christmas Bonus and other benefits received by each employee.

In fine, petitioner is liable to pay deficiency WTC on the Performance Bonus in the amount of ₱6,436,115.47 and Christmas Bonus in the amount of ₱6,005,250.00 based on the graduated tax rates of 5% to 32%. However, the employees to whom the compensation pertained to were not individually identified. Consequently, the BIR used the highest tax rate of 32% in computing the deficiency WTC. In the absence of a detailed list of employees with their corresponding 13th Month, Performance Bonus, Christmas Bonus and Other Benefits for the year 2004, the appropriate tax rate to be used should be the effective rate computed based on the total withholding tax on compensation paid divided by the total amount of taxable compensation reported during the taxable year 2004, as shown hereinbelow:

Total Withholding Tax on Compensation	₱ 77,820,509.35	18.6313685%
Total Taxable Compensation Income	₱417,685,417.49	

Particulars	Taxable		Personal Exemption	Net Taxable Compensation Income	Tax Due
	13th Month & Other Benefits	Gross Income			
Regular Employees page 747 BIR Records	1,489,820.83	379,517,613.72	60,170,000.00	320,837,434.55	62,021,116.27
Regular Employees page 732 BIR Records	1,355.00	56,843,291.53	9,622,000.00	47,222,646.53	7,001,332.67
Resigned Employees page 719 BIR Records	-	28,339,570.81	9,792,000.00	18,547,570.81	2,841,377.93
Resigned Employees page 714 BIR Records	-	6,543,939.21	2,096,000.00	4,447,939.21	576,422.49
Casual Employees page 728 BIR Records	-	2,623,619.03	-	2,623,619.03	203,500.42
Resigned Casual Employees	-	4,675,241.02	3,231,000.00	1,444,241.02	165,696.14
Casual Employees page 729 BIR Records	-	1,874,964.04	902,000.00	972,964.04	99,727.09
Extension Clinic (Exhibit "MM")	5,807,864.01	18,844,138.29	3,063,000.00	21,589,002.30	4,911,336.34
				417,685,417.49	**77,820,509.35**

Thus, petitioner's basic deficiency WTC for the taxable year 2004 on Performance and Christmas Bonus amounts to ₱2,317,996.65, computed as follows:

	Amount	WTC Rate	WTC Due
Performance Bonus	₱ 6,436,115.47	18.6313685%	₱ 1,199,136.39
Christmas Bonus	6,005,250.00	18.6313685%	1,118,860.26
Total	**₱12,441,365.47**		**₱2,317,996.65**

2. Residents and Interns Accounts

Petitioner contends that resident doctors are not subject to withholding tax on compensation because they are not employees of petitioner. They are also not subject to withholding tax on professional fees because their relationship with petitioner is that of a "*trainor-trainee*".

Petitioner also avers that pursuant to Department of Health (DOH) Administrative Order No. 24, hospitals registered with the DOH as a teaching and training hospital (Tertiary Care Level with accredited training residency program for physicians) are allowed to accept doctors for residency training. Petitioner claims that it is recognized and accredited by the DOH as a Tertiary Care Level Hospital. As such, petitioner is allowed to conduct "residency training" programs.

Petitioner further alleges that the residents admitted into its program are given minimal amounts which are merely *de minimis* stipends or allowances for their minimum subsistence and as such, not subject to any withholding tax.

Petitioner argues that even assuming *arguendo* that the amounts given to its residents and interns are subject to withholding tax, respondent erroneously applied the rate of 32%. Even if an employer-employee relationship exists between petitioner and its resident doctors, the withholding tax rate is not 32% automatically. On the other hand, if a resident doctor is deemed a professional subject to withholding tax, the proper rate is 10% or 15%, as the case may be.

As found by the Independent CPA, the Residents and Interns Accounts comprised of the following[47]:

Resident Doctors Account	₱ 21,795,914.73
Interns Account	124,800.00
Total	**₱21,920,714.73**

A perusal of petitioner's Collective Bargaining Agreement[48] for the years 2000 to 2005 disclosed that petitioner's resident physicians, fellows and interns are not under its employ. As such, any remuneration given by petitioner for services rendered by the resident physicians, fellows and interns shall be subject to expanded withholding tax instead of withholding tax on compensation.

Based on the Summary of Doctors[49] and Summary of Interns[50] provided by petitioner, individual income payments made to the resident doctors and interns do not exceed ₱720,000.00. Thus, the total amount of ₱21,920,714.73 shall be subject to 10% EWT in the amount of ₱2,192,071.47 pursuant to Section 2.57.2 of RR No. 2-98, as amended by RR No. 30-03.

To recapitulate, petitioner is liable for deficiency WTC in the amount of ₱2,317,996.65 and deficiency EWT of ₱2,951,334.53 (*in addition to the deficiency EWT of ₱10,406,489.93 found earlier under the deficiency EWT assessment*), as shown below:

Deficiency EWT		
Performance	₱ 759,263.06	
Residents and Interns	2,192,071.47	**₱2,951,334.53**

[47] Exhibit "Y-5".
[48] Exhibits "NNNNN" and "NNNNN-1".
[49] Exhibit "D5".
[50] Exhibit "C5".

Deficiency WTC		
Performance Bonus	₱1,199,136.39	
Christmas Bonus	1,118,860.26	**₱2,317,996.65**

C. DEFICIENCY INCOME TAX - ₱237,079,523.66

Respondent assessed petitioner for deficiency income tax for the taxable year 2004 on the basis of Section 27(B) of the NIRC of 1997, as amended, which provides:

> "SEC. 27. *Rates of Income Tax on Domestic Corporations.* –
>
> xxx xxx xxx
>
> (B) *Proprietary Educational Institutions and Hospitals.* - Proprietary educational institutions and hospitals which are nonprofit shall pay a tax of ten percent (10%) on their taxable income except those covered by Subsection (D) hereof: *Provided*, that if the gross income from unrelated trade, business or other activity exceeds fifty percent (50%) of the total gross income derived by such educational institutions or hospitals from all sources, the tax prescribed in Subsection (A) hereof shall be imposed on the entire taxable income. For purposes of this Subsection, the term **'unrelated trade, business or other activity'** means any trade, business or other activity, the conduct of which is not substantially related to the exercise or performance by such educational institution or hospital of its primary purpose or function. A **'proprietary educational institution'** is any private school maintained and administered by private individuals or groups with an issued permit to operate from the Department of Education, Culture and Sports (DECS), or the Commission on Higher Education (CHED), or the Technical Education and Skills Development Authority (TESDA), as the case may be, in accordance with existing laws and regulations."

In the Details of Discrepancies [51] for petitioner's deficiency income tax, respondent argues that the hospital's operations indicate that it is established for profit and not solely for charitable or social welfare purposes and that the hospital's board of trustees, officers and employees directly benefit from the profits and assets of the corporation.

Respondent likewise asserts that petitioner's accounting records show that it is not operated purely for charitable or social welfare purposes. In fact, services rendered for this purpose referred to by petitioner as "free services" represent only twelve percent (12%) of its operations, while the remaining eighty-eight percent (88%) are revenues from services rendered to paying patients. The free services are mostly availed of by hospital employees and their dependents.

Respondent further explains that pharmacy items/medicines sold by petitioner have a much higher rate than the prevailing market price and that the premises of the hospital would show that more bed capacity are allocated to paying patients. In fact, petitioner has already earned a reputation for being a hospital only for the rich and the privileged mainly because of the prohibitive price structure of its hospital services. Respondent concludes that the majority of petitioner's receipts are derived from paying patrons clearly indicating that the hospital is really established for profit and therefore should not be granted exemption.

On her second argument, respondent contends that Section 30(E) of the NIRC of 1997, as amended, provides that no part of the income or asset of the non-stock corporation or association organized and operated exclusively for religious, charitable, scientific, athletic, or cultural purposes or for the rehabilitation of veterans **shall belong to or inure to the benefit of any member, organizer, officer or any specific person**. However, petitioner's practices, as revealed by the investigation, prove

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[51] Exhibit "X".

that petitioner's board of trustees, officers and employees directly benefited from its profits and assets, which is a direct contravention of the very provision where the taxpayer anchors its own argument for exemption.

Out of the total operating expenses of ₱2,663,701,496.14, petitioner spent 29.02% or ₱773,141,824.85 for remuneration and other benefits to its officers and employees; not to mention the cost of medical benefits being extended to the same group of people in the form of discounts, ranging from a low of 20% to a high of 100% for medical services and medicines.

Petitioner counters that it is exempt from income tax on the basis of Section 30(E) and (G) of the NIRC of 1997, as amended, which provides:

> "SEC. 30. *Exemptions from Tax on Corporations.* – The following organizations shall not be taxed under this Title in respect to income received by them as such:
>
> xxx xxx xxx
>
> (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;
>
> xxx xxx xxx
>
> (G) Civic league or organization not organized for profit but operated exclusively for the promotion of social welfare; xxx"

Further, petitioner argues that Section 27(B) of the NIRC of 1997, as amended, applies only to hospitals organized and registered as non-profit hospitals and that there is nothing in the said Section which removes hospitals organized and registered as charitable and social welfare institutions from the coverage of Section 30(E) and (G) of the NIRC of 1997, as amended.

Petitioner likewise explains that while the NIRC of 1997, as amended, does not give the definition for a charitable and social welfare institution in order to be covered by Section 30(E) and (G) of the NIRC of 1997, as amended, however, the Supreme Court, in the case of *Lung Center of the Philippines vs. Quezon City, et al.*[52] has laid down the definition of a **charitable and social welfare institution**, to wit:

> "(T)o determine whether an enterprise is a charitable institution/entity or not, the elements which should be considered include the statute creating the enterprise, its corporate purposes, its constitution and by-laws, the methods of administration, the nature of the actual work performed, the character of the services rendered, the indefiniteness of the beneficiaries, and the use and occupation of the properties."

Considering the foregoing definition, petitioner points out that it possesses the characteristics of a "charitable" institution and thus falls under the coverage of Section 30(E) and (G) of the NIRC of 1997, as amended, namely:

1. That it was incorporated and is recognized as a non-stock, non-profit institution organized for charitable and social welfare purposes;
2. That its operation as a hospital is not an activity that is conducted strictly for profit, but an activity that by its very purpose is charitable;
3. That substantial portions of its transactions are attributable to the pursuit of charitable and social welfare activities;

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[52] G.R. No. 144104, June 29, 2004.

4. That it extends its medical services to and utilizes its facilities for all patients without discrimination; and
5. That no part of its net income and/or net assets inures to the private benefit of the persons managing or operating the hospital.

Nevertheless, petitioner contends that it is still possible to reconcile the provisions of Section 27(B) with Section 30 of the NIRC of 1997, as amended. Petitioner explains that Section 27(B) is the general rule which provides that non-profit hospitals shall be subject to income tax of 10%; while Section 30 is the exception to the rule which provides exemption from the income tax of hospitals that are non-profit, but organized as non-stock corporations for any or more of the purposes described in Section 30 of the NIRC of 1997, as amended.

To prove that it is covered by Sections 30(E) and (G), petitioner claims that it is organized as a non-stock, non-profit corporation for charitable and social welfare purposes, as provided in its Articles of Incorporation[53], the pertinent parts of which are quoted hereunder:

> "That the objects and purposes for which the corporation is formed are:
>
> (a) To establish, equip, operate and maintain a non-stock, non-profit Christian, benevolent, charitable and scientific hospital which shall give curative, rehabilitative and spiritual care to sick, diseased and disabled persons; provided that purely medical and surgical services shall be performed by duly licensed physicians and surgeons who may be freely and individually contracted by the patients;"

Petitioner also contends that respondent has acknowledged the fact that it is organized and operated as a charitable and social welfare institution as proved by the

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[53] Exhibits "G" and "G-1".

Letter of Exemption that respondent issued on June 6, 1990[54], to wit:

> "xxx this Office is of the opinion and so holds that the St. Luke's Medical Center, Inc. falls within the purview of a corporation for purely charitable and social welfare purposes as contemplated under Section 26(e) and (g) [now Section 30] of the [NIRC] as amended. Accordingly, it is exempt from the payment of income tax on income received by it as such organization, and therefore, need not file an income tax return concerning such income. xxx."

Petitioner also points out that respondent issued Certificate of Registration No. 010-2001 dated February 2, 2001[55], certifying its status as an accredited donee institution. The said Certificate of Registration was even renewed by respondent for another period of five (5) years after its expiration.[56]

Moreover, petitioner states that it is a member of the National Council for Social Development[57] which, among others, requires that a member entity must be organized for charitable or social welfare purposes. Petitioner was likewise recognized by the Department of Social Welfare and Development[58] and was granted endowment funds by the Philippine Charity Sweepstakes Office[59]. Petitioner further alleges that it is actively involved in providing charitable and social welfare activities with local governments and their constituents as shown by several municipal resolutions and letters of appreciation[60], as well as several Agreements extending assistance to hospitals and other health-related institutions, including local government hospitals[61]. ℒ

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[54] Exhibits "H" and "H-1".
[55] Exhibit "I".
[56] Exhibit "J".
[57] Exhibits "K", "L", and "M".
[58] Exhibit "N".
[59] Exhibit "V"
[60] Exhibits "O", "Q", "R", "S", "T", "TT", "UU", "VV", "YY", "ZZ", "BBB", "DDD", "TTT", "XXX" to "YYY-1", "AAAA", "BBBB", and "DDDD".
[61] Exhibits "P", "U", "AAA", "EEE", "FFF", "GGG", "HHH", and "RRR" to "SSS".

Lastly, petitioner maintains that no part of its net income or assets inures to the benefit of any private individual or person as contemplated by law. After all, its officers and employees receive salaries for the services they rendered to the hospital and its trustees receive no remuneration.

Considering the respective arguments of the parties, this Court finds petitioner liable for deficiency income tax for the taxable year 2004 as provided by Section 27(B) of the NIRC of 1997, as amended.

The Court of Tax Appeals *En Banc* in the case of *Commissioner of Internal Revenue vs. St. Luke's Medical Center, Inc.*[62], adopting the ruling of the Supreme Court in the case of *Commissioner of Internal Revenue vs. St. Luke's Medical Center, Inc.*[63], had the occasion to explain the reason for imposing income tax on petitioner despite its claim that it is exempted by virtue of being a non-stock, non-profit corporation organized and operated for charitable and social welfare purposes, to wit:

> "*First*, the Supreme Court described the rate of tax imposed under Section 27 (B), the qualifications of hospitals in order for the said rate to apply, the effect of the introduction of the aforesaid section, and likewise explained that Section 27 (B) and Section 30 (E) and (G) of the NIRC of 1997 can be construed together without the removal of such tax exemption under the latter provision, *i.e.*, a proprietary non-profit hospital whose income **from activities conducted for profit** is subjected to the 10% tax rate under Section 27 (B) may still retain its tax exempt status under Section 30 (E) and (G) for its **not-for-profit activities**, *thus*:
>
> > 'The Court partly grants the petition of the BIR but on a different ground. We hold that Section 27(B) of the NIRC does not remove the income tax exemption of proprietary non-profit

62 CTA EB No. 823 (CTA Case No. 7857), December 3, 2012.
63 G.R. Nos. 195909 and 195960, September 26, 2012.

hospitals under Section 30(E) and (G). Section 27(B) on one hand, and Section 30(E) and (G) on the other hand, can be construed together without the removal of such tax exemption. The effect of the introduction of Section 27(B) is to subject the taxable income of two specific institutions, namely, proprietary non-profit educational institutions and proprietary non-profit hospitals, among the institutions covered by Section 30, to the 10% preferential rate under Section 27(B) instead of the ordinary 30% corporate rate under the last paragraph of Section 30 in relation to Section 27(A)(1).

'Section 27(B) of the NIRC imposes a 10% preferential tax rate on the income of (1) proprietary non-profit educational institutions and (2) proprietary non-profit hospitals. The only qualifications for hospitals are that they must be proprietary and non-profit. 'Proprietary' means private, following the definition of a 'proprietary educational institution' as 'any **private** school maintained and administered by **private** individuals or groups' with a government permit. 'Non-profit' means no net income or asset accrues to or benefits any member or specific person, with all the net income or asset devoted to the institution's purposes and all its activities.' (Underscoring supplied)

Second, the High Court discussed Section 30 (E) and (G) of the NIRC of 1997, as amended, *(the provision under which the respondent SLMCI is claiming income tax exemption)* by enumerating the essential requisites in order for the income received by a charitable corporation or association to be considered exempt from income tax. The discussion highlights the High Court's pronouncement that *'[t]o be exempt from income taxes, Section 30(E) of the NIRC requires that a charitable institution must be* ***'organized and operated exclusively'*** *for charitable purposes. Likewise, to be exempt from income taxes, Section 30 (G) of the NIRC requires that the institution be operated exclusively 'for social welfare.' viz:*

'Section 30(E) of the NIRC provides that a charitable institution must be:

(1) A non-stock corporation or association;
(2) **Organized exclusively** for charitable purposes;
(3) **Operated exclusively** for charitable purposes; and
(4) 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.

'Thus, both the organization and operations of the charitable institution must be devoted **'exclusively'** for charitable purposes. The organization of the institution refers to its corporate form, as shown by its articles of incorporation, by-laws and other constitutive documents. Section 30 (E) of the NIRC specifically requires that the corporation or association be non-stock, which is defined by the Corporation Code as 'one where no part of its income is distributable as dividends to its members, trustees, or officers' and that any profit 'obtain[ed] as an incident to its operations shall, whenever necessary or proper, be used for the furtherance of the purpose or purposes for which the corporation was organized.' However, under *Lung Center*, any profit by a charitable institution must not only be plowed back 'whenever necessary or proper,' but must be 'devoted or used **altogether** to the charitable object which it is intended to achieve.'

'The operations of the charitable institution generally refer to its regular activities. Section 30(E) of the NIRC requires that these operations be **exclusive** to charity. There is also a specific requirement that 'no part of [the] net income or asset shall belong to or inure to the benefit of any member, organizer, officer or any specific person.' The use of lands, buildings and improvements of the institution is but a part of its operations.

'There is no dispute that St. Luke's is organized as a non-stock and non-profit charitable institution. However, this does not

> automatically exempt St. Luke's from paying taxes. This only refers to the organization of St. Luke's. Even if St. Luke's meets the test of charity, a charitable institution is not *ipso facto* tax exempt. xxx. To be exempt from income taxes, Section 30(E) of the NIRC requires that a charitable institution must be **'organized and operated exclusively'** for charitable purposes. Likewise, to be exempt from income taxes, Section 30(G) of the NIRC requires that the institution be operated exclusively 'for social welfare.'

Following the foregoing discussion, the Supreme Court keenly steered the discussion to the last paragraph of Section 30 of the NIRC and stressed its point that this last paragraph qualifies the words 'organized and operated exclusively' by providing that *'income of whatever kind and character of the foregoing organizations ... 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****.'* Simply put, even if the charitable institution must be **'organized and operated exclusively'** for charitable purposes, it is still allowed to engage in **'activities conducted for profit'** without losing its tax exempt status for its **not-for-profit activities**. The only consequence is that the **'income of whatever kind and character'** of a charitable institution **'from any of its activities conducted for profit, regardless of the disposition made of such income, shall be subject to tax.'**, *viz:*

> 'However, the last paragraph of Section 30 of the NIRC qualifies the words 'organized and operated exclusively' by providing that: 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**.

'In short, the last paragraph of Section 30 provides that if a tax exempt charitable institution conducts **'any'** activity for profit, such activity is not tax exempt even as its not-for-profit activities remain tax exempt. This paragraph qualifies the requirements in Section 30(E) that the '[n]on–stock corporation or association [must be] **organized and operated exclusively** for ... charitable ... purposes ....' It likewise qualifies the requirement in Section 30(G) that the civic organization must be 'operated exclusively' for the promotion of social welfare.

'Thus, even if the charitable institution must be 'organized and operated exclusively' for charitable purposes, it is nevertheless allowed to engage in 'activities conducted for profit' without losing its tax exempt status for its not-for-profit activities. The only consequence is that the **'income of whatever kind and character'** of a charitable institution **'from any of its activities conducted for profit, regardless of the disposition made of such income, shall be subject to tax.'** Prior to the introduction of Section 27(B), the tax rate on such income from for-profit activities was the ordinary corporate rate under Section 27(A). With the introduction of Section 27(B), the tax rate is now 10%.' (Underscoring supplied)

Finally, consistent with the above-discussion, the Supreme Court held that St. Luke's is a corporation that is not **'operated exclusively'** for charitable or social welfare purposes insofar as its revenues from paying patients are concerned. The Supreme Court declared that the P1.73 billion from paying patients are income received from **'activities conducted for profit'**. The Supreme Court explained, *thus:*

'In 1998, St. Luke's had total revenues of P1,730,367,965 from services to *paying* patients. It cannot be disputed that a hospital which receives approximately P1.73 billion from **paying** patients is **not** an institution 'operated exclusively' for charitable purposes. Clearly,

> revenues from **paying** patients are income received from 'activities conducted for profit.' ...
>
> xxx xxx xxx
>
> 'In *Lung Center*, this Court declared:
>
> > '[e]xclusive' is defined as possessed and enjoyed to the exclusion of others; debarred from participation or enjoyment; and 'exclusively' is defined, 'in a manner to exclude; as enjoying a privilege exclusively.' ... The words 'dominant use' or 'principal use' cannot be substituted for the words 'used exclusively' without doing violence to the Constitution and the law. **Solely is synonymous with exclusively**.
>
> 'The Court cannot expand the meaning of the words 'operated exclusively' without violating the NIRC. **Services to paying patients are activities conducted for profit. They cannot be considered any other way. There is a 'purpose to make profit over and above the cost' of services**. The P1.73 billion total revenues from paying patients is not even incidental to St. Luke's charity expenditure of P218,187,498 for non-paying patients.
>
> 'St. Luke's claims that its charity expenditure of P218,187,498 is 65.20% of its operating income in 1998. However, if a part of the remaining 34.80% of the operating income is reinvested in property, equipment or facilities used for services to **paying and non-paying patients**, then it cannot be said that the income is 'devoted or used **altogether** to the charitable object which it is intended to achieve.' The income is plowed back to the corporation not entirely for charitable purposes, but for profit as well. In any case, the last paragraph of Section 30 of the NIRC expressly qualifies that income from activities for profit is taxable '**regardless of the disposition made of such income**.'
>
> xxx xxx xxx

> 'The Court finds that St. Luke's is a corporation that is **not** 'operated exclusively' for charitable or social welfare purposes insofar as its revenues from paying patients are concerned. <u>This ruling is based not only on a strict interpretation of a provision granting tax exemption, but also on the clear and plain text of Section 30(E) and (G). Section 30(E) and (G) of the NIRC requires that an institution be **'operated exclusively'** for charitable or social welfare purposes to be **completely** exempt from income tax</u>. An <u>institution under Section 30(E) or (G) does not lose its tax exemption if it earns income from its for-profit activities. Such income from for-profit activities, under the last paragraph of Section 30, is merely subject to income tax, previously at the ordinary corporate rate but now at the preferential 10% rate pursuant to Section 27(B)</u>.
>
> xxx xxx xxx
>
> 'St. Luke's fails to meet the requirements under Section 30(E) and (G) of the NIRC to be completely tax exempt from all its income. However, it remains a proprietary non-profit hospital under Section 27(B) of the NIRC as long as it does not distribute any of its profits to its members and such profits are reinvested pursuant to its corporate purposes. St. Luke's, as a proprietary non-profit hospital, is entitled to the preferential tax rate of 10% on its net income from its for-profit activities.' (Underscoring supplied)

Conspicuously, the present case fits perfectly into the mold of the above-quoted case entitled *Commissioner of Internal Revenue vs. St. Luke's Medical Center, Inc.*, G.R. No. 195909 and 195960, September 26, 2012. The facts in the instant case, the issue, and laws applicable, and even the parties involved are substantially similar to those of G.R. No. 195909. Thus, applying the foregoing principles laid down by the Supreme Court in G.R. No. 195909 to the instant case, the inescapable conclusion is that respondent SLMCI is liable for deficiency income tax in 2007 under Section 27 (B) of the NIRC of 1997, as amended."

A perusal of the records would show that the instant case is on all fours with the above-quoted ruling of this Court *En Banc* in the case of *Commissioner of Internal Revenue vs. St. Luke's Medical Center, Inc.*[64], citing the Supreme Court's Decision in the case of *Commissioner of Internal Revenue vs. St. Luke's Medical Center, Inc.*[65]. Thus, applying the principles laid down by the Supreme Court to the instant case, petitioner is liable for deficiency income tax at 10% preferential rate for the taxable year 2004 under Section 27(B) of the NIRC of 1997, as amended.

Respondent's examiner computed the deficiency income tax assessment for the taxable year 2004 in the amount of ₱237,079,523.66 as follows:[66]

Sales/Revenue	₱ 3,323,196,110.00
Less: Cost of Service	2,384,876,987.00
Gross Income from Operation	938,319,123.00
Add: Other Income	90,199,463.00
Total Gross Income	1,028,518,586.00
Less: Deduction	269,192,114.00
Taxable Income	759,326,472.00
Add: Disallowed Expenses	
Bad Debts (acct code 200052) part of free service (RR 5-99)	18,042,796.43
Expenses not subjected to EWT	
Expenses subject to 1% EWT	501,834,595.16
Expenses subject to 2% EWT	109,310,955.91
Rent Expense subject to 5% EWT	8,323,596.67
Professional Fees (H.O.) not subjected to W/holding Tax	58,403,053.37
Professional Fees (E.O.) not subjected to W/holding Tax	3,665,261.30
Honorarium not subjected to W/holding Tax (BIR Ruling 43-2001 & RMC 72-2004)	16,547,526.51
Christmas bonus for the year 2004 (RR 2-98 Sec. 2.78.1(b)(ii))	39,941,312.37
Residents and Interns (no withholding tax) (RR 2-98 Sec.2.78.1 (A))	21,822,856.25
Total Taxable Income	₱ 1,537,218,425.97
Tax due at 10%	153,721,842.60
Interest from (4/16/05 to 12/31/07)	83,332,681.06
Compromise	25,000.00
Total amount due and collectible	**₱ 237,079,523.66**

Petitioner avers that even assuming that it is liable for income tax for the taxable year 2004, respondent erred in computing the same. Petitioner maintains that respondent

[64] CTA EB No. 823, December 3, 2012.
[65] G.R. Nos. 195909 and 195960, September 26, 2012.
[66] Exhibit "W".

simply referred to its gross income appearing in its Income Tax Return and subtracted therefrom the allowed deductions without considering that its total gross income is the sum of gross revenues from its hospital operations and other unrelated income. The said unrelated income, such as petitioner's interest income, investment income from government securities, trust fund and mutual funds, have already been subjected to the corresponding withholding taxes or are exempt from tax, thus, should be excluded in determining the net income subject to tax.

Petitioner asserts that from the total "Other Income" of ₱90,199,463.00, the following must be excluded in the computation of gross income:

Interest Income subjected to Final Tax	₱ 76,155,703.64
Interest Income constructively received subjected to Final Tax	141,335.62
Realized Gain on Investment in Trust Fund subjected to Final Tax	6,055.46
Foreign Exchange Gain/(Loss) exempted from tax	13,012,554.51
Dividend Income subjected to Final Tax	64,800.00
Total	**₱89,380,449.23**

Petitioner submitted its Other Income (Expense) Schedule [67], Schedule of Investments in Trust Funds, Financial Reports, and other supporting investing schedules [68], and relevant documents such as journal voucher, journal entries, passbooks, and other schedules[69].

Based on the Court's examination of the aforesaid documents, only the amount of ₱3,685,883.64 was ascertained to be pertaining to petitioner's interest income subjected to final tax, detailed as follows:

INVESTMENT IN TRUST FUND			
Bank	**Month**	**Interest Income**	**Exhibit**
Bank of the Philippine Islands – ALFI	January	287,882.77	"O4-1"
	February	278,898.38	

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[67] Exhibit "O^4".
[68] Exhibit "O^4-1".
[69] Exhibit "O^4-2".

	March	298,132.76	
	April	278,265.58	
	May	298,132.76	
	June	278,265.57	
	July	298,132.76	
	August	287,882.76	
	September	278,265.58	
	October	265,178.43	
	November	246,183.73	
	December	264,777.05	
	Subtotal	**3,359,998.13**	
PESO SAVINGS ACCOUNT			
Bank	**Month**	**Interest Income**	**Exhibit**
Security Bank Corporation	December	51,210.66	"O4-2-270"
International Exchange Bank	March	82,960.69	"O4-2-103"
	June	83,327.65	"O4-2-195"
Asiatrust Bank	April	970.22	"O4-2-100"
	May	1,106.84	"O4-2-147"
Bank of the Philippine Islands	June	39,650.45	"O4-2-197"
Equitable PCI Bank	June	32,757.73	"O4-2-189"
	Subtotal	**291,984.24**	
DOLLAR SAVINGS ACCOUNT			
Bank	**Month**	**Interest Income**	**Exhibit**
Security Bank Corporation	December	23,904.93	"O4-2-254"
International Exchange Bank	December	9,795.53	"O4-2-267"
Bank of the Philippine Islands	June	113.26	"O4-2-186"
United Coconut Planters Bank	June	87.55	"O4-2-184"
	Subtotal	**33,901.27**	
TOTAL		**3,685,883.64**	

The Court thus sustains respondent's assessment on "Other Income", but in the reduced amount of ₱86,513,579.36 *(₱90,199,463.00 minus ₱3,685,883.64).*

In arriving at the deficiency income tax assessment, respondent disallowed petitioner's claimed expense deductions, namely:

1. Bad Debts	₱ 18,042,796.43

ℓ

2. Expenses not subjected to EWT	
Expenses subject to 1% EWT	501,834,595.16
Expenses subject to 2% EWT	109,310,955.91
Rent Expense subject to 5% EWT	8,323,596.67
Professional Fees (H.O.) not subjected to W/holding Tax	58,403,053.37
Professional Fees (E.O.) not subjected to W/holding Tax	3,665,261.30
Honorarium not subjected to W/holding Tax	16,547,526.51
Christmas bonus for the year 2004	39,941,312.37
Residents and Interns Salaries	21,822,856.25

The Court shall determine the propriety of each disallowed expense.

1. Bad debts

Bad debts expense amounting to ₱18,042,796.43 was disallowed by respondent for failure to show strong proof that the bad debts are already worthless or uncollectible, pursuant to Section 34(E)(1) of the NIRC, as amended, in relation to Revenue Regulations No. 5-99.

Petitioner explains that it exerted all efforts to collect such bad debts. These bad debts are recorded as valid bad debts on its books and are existing debts of patients who could not or refused to pay. They are essentially connected to its operations as a hospital. These debts were actually charged off from the books of accounts at the end of the taxable year.

Section 34(E) of the NIRC of 1997, as amended, provides as follows:

> "SEC. 34. *Deductions from Gross Income.* -
>
> (E) *Bad Debts.-*
>
> (1) *In General.* - Debts due to the taxpayer actually ascertained to be worthless and charged off within the taxable year except those not connected with profession, trade or business and those sustained

> in a transaction entered into between parties mentioned under Section 36(B) of this Code: xxx"

Relative thereto, RR No. 25-02, amending RR No. 05-99 and implementing the above provision, provides the requisites for valid deduction of bad debts from gross income, thus:

> "SECTION 2. *Amendment.* - Section 3 of RR 5-99 on the requisites for valid deduction of bad debts from gross income is hereby amended by deleting the penultimate paragraph of the said Section and should now read as follows:
>
>> 'Sec. 3. *Requisites for valid deduction of bad debts from gross income.* - The requisites for deductibility of bad debts are:
>>
>> (1) There must be an existing indebtedness due to the taxpayer which must be valid and legally demandable;
>>
>> (2) The same must be connected with the taxpayer's trade, business or practice of profession;
>>
>> (3) The same must not be sustained in a transaction entered into between related parties enumerated under Sec. 36(B) of the Tax Code of 1997;
>>
>> (4) The same must be actually charged off the books of accounts of the taxpayer as of the end of the taxable year; and
>>
>> (5) The same must be actually ascertained to be worthless and uncollectible as of the end of the taxable year."

Additionally, before a bad debt can be considered worthless, the taxpayer must also show that it is indeed uncollectible even in the future. Furthermore, there are steps outlined to be undertaken by the taxpayer to prove that he exerted diligent efforts to collect the debts, to wit: (1) sending statements of accounts; (2) sending of collection letters; (3) giving the account to a lawyer for collection; and (4) filing a collection case in court.[70]

The fact that petitioner complied with the first four requisites is not disputed. What is put in issue is whether or not the amount of ₱18,042,796.43 has become worthless or uncollectible.

Petitioner submitted its Schedule of Bad Debts Expenses[71], General Policy of Writing-off worthless or uncollectible accounts (Billing and Accounts Service Department)[72] and the Report of SLMC's Billing and Accounts Services Department[73] on means employed to collect bad debts that have been written off. However, these documents merely outline the steps to be taken by the Billing and Accounts Service Department in the collection of its outstanding receivables and do not prove that petitioner exerted earnest efforts to collect the subject amount of ₱18,042,796.43. For failure to show sufficient proof that there is no likelihood of recovering the amount of ₱18,042,796.43 at any time in the future, petitioner cannot validly deduct the said amount from its gross income.

2. Expenses not subjected to EWT

Based on the finding that petitioner failed to withhold and remit the required EWT and WTC on the income payments enumerated hereinbelow pursuant to Section 2.57.2 of RR No. 02-98 in relation to Sections 57 and 79 of the NIRC of 1997, as amended, respondent disallowed the same from petitioner's deductible expenses in accordance with Section 34(K) of the same Code: c

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[70] *Philippine Refining Company (now known as "Unilever Philippines [PRC], Inc.") vs. Court of Appeals, et al.,* G.R. No. 118794, May 8, 1996.
[71] Exhibit "P-4".
[72] Exhibit "P4-1".
[73] Exhibit "JJ".

Expenses not subjected to EWT and WTC	
Expenses subject to 1% EWT	₱ 501,834,595.16
Expenses subject to 2% EWT	109,310,955.91
Rent Expense subject to 5% EWT	8,323,596.67
Professional Fees (Main Hospital)	58,403,053.37
Professional Fees (Extension Clinic)	3,665,261.30
Honorarium	16,547,526.51
Christmas bonus for the year 2004	39,941,312.37
Residents and Interns Accounts	21,822,856.25

Anent the disallowed expenses subject to 1%, 2% and 5% EWT in the respective amounts of ₱501,834,595.16, ₱109,310,955.91 and ₱8,323,596.67, as discussed earlier under the deficiency EWT assessment *(item A.2)*, petitioner failed to prove that it withheld and remitted the EWT on the total expenses of ₱482,594,339.74, broken down hereinbelow:

	Local Supplier of Goods (1%)	Contractors/ Subcontractors (2%)	Rent (5%)	Total
Income Payments	371,633,787.16	109,310,955.91	1,649,596.67	482,594,339.74
EWT Due	3,716,337.87	2,186,219.12	82,479.83	5,985,036.82

Consequently, the amount of ₱482,594,339.74 shall be disallowed from petitioner's claimed deductible expenses pursuant to Section 34(K) of the NIRC of 1997, as amended, which states that:

> "(K) *Additional Requirements for Deductibility of Certain Payments*. - Any amount paid or payable which is otherwise deductible from, or taken into account in computing gross income or for which depreciation or amortization may be allowed under this Section, shall be allowed as a deduction only if it is shown that the tax required to be deducted and withheld therefrom has been paid to the Bureau of Internal Revenue in accordance with this Section, sections 58 and 81 of this Code."

As regards the disallowed Professional Fees for petitioner's Main Hospital and Extension Clinic in the respective amounts of ₱58,403,053.37 and ₱3,665,261.30, as discussed earlier under the deficiency EWT assessment *(item A.1)*, the EWT rate used by petitioner for some Professional Fees exceeding ₱720,000.00 was 10% instead of 15%, thus, there was underwithholding of 5%. Professional Fees not subjected to EWT amounted to ₱13,624,827.47, computed as follows:

PROFESSIONAL FEES (MAIN HOSPITAL)							
Payee		**Income Payments**	**Tax Rate for Income Payments exceeding ₱720,000.00**	**Tax Due**	**Tax Paid**	**Tax Still Due**	**Income Payments not Subjected to EWT**
Bondoc	Edgardo	1,597,969.37	15%	239,695.41	202,378.80	37,316.61	248,777.37
Calleja	Homobono	1,884,093.83	15%	282,614.07	239,172.81	43,441.26	289,608.43
Cervantes	Julieta	1,272,032.67	15%	190,804.90	151,414.51	39,390.39	262,602.60
Cuanang	Joven	1,702,800.70	15%	255,420.11	179,245.00	76,175.11	507,834.03
De Castro	Estanislao	3,848,845.03	15%	577,326.75	514,233.64	63,093.11	420,620.76
Dy	Pilar	2,989,345.20	15%	448,401.78	410,978.94	37,422.84	249,485.60
Eduardo	Emmanuel	2,227,042.90	15%	334,056.44	286,264.55	47,791.89	318,612.57
Estrera	Dahlia Virgina	2,294,127.27	15%	344,119.09	300,828.55	43,290.54	288,603.60
Joson	Rafael	7,058,124.47	15%	1,058,718.67	981,526.58	77,192.09	514,613.94
Kuizon	Danilo	1,868,541.03	15%	280,281.15	240,484.21	39,796.94	265,312.96
Lazatin	Benedict	2,508,234.20	15%	376,235.13	336,461.34	39,773.79	265,158.60
Lazo	Henry	8,212,900.17	15%	1,231,935.03	1,127,709.53	104,225.50	694,836.64
Lo	Raymundo	5,372,726.30	15%	805,908.95	735,446.00	70,462.94	469,752.97
Lopez	Rolando	3,780,462.73	15%	567,069.41	515,384.57	51,684.84	344,565.60
Miranda	Ariel	3,526,225.73	15%	528,933.86	481,047.43	47,886.43	319,242.86
Narciso	Francisco	4,769,782.17	15%	715,467.33	653,039.11	62,428.22	416,188.10
Ramos	Roberto	7,118,230.00	15%	1,067,734.50	989,202.41	78,532.09	523,547.27
Reyes	Augusto	1,051,835.20	15%	157,775.28	108,476.00	49,299.28	328,661.87
Rogelio	Gregorio	2,714,432.80	15%	407,164.92	369,529.37	37,635.55	250,903.67
Santiago	Jonas	2,456,371.47	15%	368,455.72	330,175.51	38,280.21	255,201.40
Serrano	Vivian	1,475,031.63	15%	221,254.74	183,321.04	37,933.70	252,891.36
Castro	Associates	1,200,000.00	15%	180,000.00	120,000.00	60,000.00	400,000.00
Yunque	Abondino	980,770.87	15%	147,115.63	98,167.84	48,947.79	326,318.60
Zamuco	Jaime	1,773,127.63	15%	265,969.14	213,509.21	52,459.93	349,732.90
						Subtotal	

c

	8,563,073.70

PROFESSIONAL FEES (EXTENSION CLINIC)							
Payee		**Income Payments**	**Tax Rate for Income Payments exceeding ₱720,000.00**	**Tax Due**	**Tax Paid**	**Tax Still Due**	**Income Payments not Subjected to EWT**
Asis	Redentor	2,012,221.80	15%	301,833.27	201,222.18	100,611.09	670,740.60
Sy	Jerry	1,009,160.70	15%	151,374.11	100,916.07	50,458.04	336,386.90
Mendoza	Merlene	966,952.00	15%	145,042.80	96,695.20	48,347.60	322,317.33
Santos	Arsenio	957,754.80	15%	143,663.22	95,775.48	47,887.74	319,251.60
Lorenzo	Juliet	957,754.80	15%	143,663.22	95,775.48	47,887.74	319,251.60
Marchandesch	Leticia	892,881.80	15%	133,932.27	89,288.18	44,644.09	297,627.27
Milo	Mario	892,128.00	15%	133,819.20	89,212.80	44,606.40	297,376.00
Tingcungco	Angelito	892,128.00	15%	133,819.20	89,212.80	44,606.40	297,376.00
Mejia	Manuel, Jr.	891,639.90	15%	133,745.99	89,163.99	44,582.00	297,213.30
Gapasin	Judith	876,111.90	15%	131,416.79	87,611.19	43,805.60	292,037.30
Cereso	Freman	860,119.20	15%	129,017.88	86,011.92	43,005.96	286,706.40
Tucay	Agnes	822,838.00	15%	123,425.70	82,283.80	41,141.90	274,279.33
Zantua	Raphael Ryan	806,941.60	15%	121,041.24	80,694.16	40,347.08	268,980.53
Tiu	Dionisio	798,661.10	15%	119,799.17	79,866.11	39,933.06	266,220.37
Griño	Lilibeth	794,922.40	15%	119,238.36	79,492.24	39,746.12	264,974.13
Payumo	Ronald Alan	753,045.30	15%	112,956.80	75,304.53	37,652.27	251,015.10
						Subtotal	**5,061,753.77**
						Total	**13,624,827.47**

Therefore, for failure to withhold and remit the corresponding EWT, petitioner cannot claim the amount of ₱13,624,827.47 Professional Fees as deduction from its gross income pursuant to Section 34(K) of the NIRC of 1997, as amended.

Similarly, the Court upholds respondent's disallowance of petitioner's claimed honorarium expense but in the reduced amount of ₱15,851,526.51 due to non-withholding of the related EWT as discussed under the deficiency EWT assessment *(item A.1)*.

As to the Performance and Christmas Bonus disallowed by respondent in the total amount of ₱39,941,312.37, as discussed earlier under the deficiency WTC assessment *(item B.1)*, there was underwithholding of 5% EWT on the ₱27,499,946.90 Performance Bonus paid by petitioner to doctors at its Extension Clinic, hence, the related Performance Bonus in the amount of ₱5,061,753.77 cannot be claimed by petitioner as deduction from its gross income. Below is the computation of the amount of ₱5,061,753.77:

Payee		Income Payments	Tax Rate for Income Payments exceeding ₱720,000.00	Tax Due	Tax Paid	Tax Still Due	Income Payments not Subjected to EWT
Asis	Redentor	2,012,221.80	15%	301,833.27	201,222.18	100,611.09	670,740.60
Cantos	Arsenio	957,754.80	15%	143,663.22	95,775.48	47,887.74	319,251.60
Cerezo	Freman	860,119.20	15%	129,017.88	86,011.92	43,005.96	286,706.40
Gapasin	Judith	876,111.90	15%	131,416.79	87,611.19	43,805.60	292,037.30
Grino	Lilibeth	794,922.40	15%	119,238.36	79,492.24	39,746.12	264,974.13
Lorenzo	Juliet	957,754.80	15%	143,663.22	95,775.48	47,887.74	319,251.60
Marchadesch	Leticia	892,881.80	15%	133,932.27	89,288.18	44,644.09	297,627.27
Mejia	Manuel Jr.	891,639.90	15%	133,745.99	89,163.99	44,582.00	297,213.30
Mendoza	Merlene	966,952.00	15%	145,042.80	96,695.20	48,347.60	322,317.33
Milo	Mario	892,128.00	15%	133,819.20	89,212.80	44,606.40	297,376.00
Payumo	Ronald Allan	753,045.30	15%	112,956.80	75,304.53	37,652.27	251,015.10
Sy	Jerry	1,009,160.70	15%	151,374.11	100,916.07	50,458.04	336,386.90
Tingcungco	Angelito	892,128.00	15%	133,819.20	89,212.80	44,606.40	297,376.00
Tiu	Dionisio	798,661.10	15%	119,799.17	79,866.11	39,933.06	266,220.37
Tucay	Agnes	822,838.00	15%	123,425.70	82,283.80	41,141.90	274,279.33
Zantua	Raphael Ryan	806,941.60	15%	121,041.24	80,694.16	40,347.08	268,980.53
Total		**15,185,261.30**		**2,277,789.20**	**1,518,526.13**	**759,263.06**	**5,061,753.77**

Likewise, Performance Bonus paid by petitioner to employees at its Extension Clinic in the amount of ₱6,436,115.47 and Christmas Bonus paid by petitioner to employees at its Main Hospital in the amount of ₱6,005,250.00 totalling ₱12,441,365.47 shall be disallowed on account of petitioner's failure to withhold the related WTC.

The same holds true with the disallowed income payments made by petitioner to its Residents and Interns in the respective amounts of ₱21,795,914.73 and ₱124,800.00 or in the sum of ₱21,920,714.73. Petitioner cannot claim the said amount as deduction from its gross income for failure to withhold the corresponding EWT.

In sum, petitioner is liable to pay basic deficiency income tax for the taxable year 2004 in the amount of ₱132,011,615.87, computed as follows:

Sales/Revenue		₱ 3,323,196,110.00
Less: Cost of Service		2,384,876,987.00
Gross Income from Operation		₱ 938,319,123.00
Add: Other Income		86,513,579.36
Total Gross Income		₱ 1,024,832,702.36
Less: Deduction		269,192,114.00
Taxable Income		₱ 755,640,588.36
Add: Disallowed Expenses		
Bad Debts		₱ 18,042,796.43
Expenses not subjected to EWT		
Expenses subject to 1% EWT	₱ 371,633,787.16	
Expenses subject to 2% EWT	109,310,955.91	
Rent Expense subject to 5% EWT	1,649,596.67	482,594,339.74
Professional Fees (H.O.)	₱ 8,563,073.70	
Professional Fees (E.O.)	5,061,753.77	13,624,827.47
Honorarium		15,851,526.51
Performance Bonus	₱ 6,436,115.47	
Christmas Bonus	6,005,250.00	12,441,365.47
Residents	₱ 21,795,914.73	
Interns	124,800.00	21,920,714.73
Total Disallowed Expenses		₱ 564,475,570.35
Total Taxable Income		₱ 1,320,116,158.71
Basic Deficiency Income Tax (10%)		**₱ 132,011,615.87**

D. DEFICIENCY VALUE-ADDED TAX - ₱1,116,454.50

Respondent's detailed computation of the deficiency VAT assessment for the taxable year 2004 in the amount of ₱10,555,169.57 is reproduced hereunder:

Taxable Receipts per return		₱ 80,112,975.20
Add: Gross rental income (Sec.108)		1,621,815.83
Write-off of long overdue payables to suppliers (part of Miscellaneous Income)		4,971,410.62
Proceeds from sale of property and equipment (Sec. 106)		317,400.00

Total VATable receipts		₱ 87,023,601.65
Output Tax due		₱ 8,702,360.17
Less: Input Tax per Audit		
Carry-over previous quarter	₱ 334,851.26	
Input from goods and services	7,654,608.49	
Total available input tax	₱ 7,989,459.75	
Less: Carry over succeeding year	(294,520.97)	7,694,938.78
VAT due		₱ 1,007,421.39
Less: Payment		316,358.75
VAT still due		₱ 691,062.64
Interest from (1/26/05 to 12/31/07)		405,391.86
Compromise		20,000.00
Total amount due and collectible		**₱ 1,116,454.50**

According to respondent, petitioner, as a hospital, is exempt from VAT on its medical and health services, including the sale of medicines to in-patients. However, the sale of medicines to out-patients is subject to VAT. During audit, respondent found that petitioner failed to pay VAT on its rental income, other income on write-off of long overdue payable to suppliers, and proceeds from the sale of property and equipment. As a consequence, respondent imposed VAT on these items pursuant to Sections 106 and 108 of the NIRC of 1997, as amended, in the amount of ₱1,116,454.50, inclusive of interest and compromise penalty.

Petitioner alleges that it incurs expenses for supplies that are used in connection with the medical services rendered by the hospital. The regular suppliers are VAT-registered and pass on the VAT to petitioner. Since petitioner cannot recognize input VAT arising from these purchases, petitioner adds it on as part of cost, and records the cost of supplies as the total amount paid to regular suppliers. In writing-off overdue accounts, petitioner merely reverses previously recorded transactions, which included VAT as part of the expense for supplies. Subjecting petitioner again to VAT (for writing-off overdue accounts from suppliers) is tantamount to double taxation. Write-off refers to reversal of the first entry (Purchases), but recognizing income instead of expense. Corollary to this is the sale of equipment, wherein VAT was recorded as part of the cost of the equipment upon the purchase.

The Court finds that petitioner's write-off of long overdue payables to suppliers is not subject to VAT because the transaction was neither a sale of goods or services nor rental derived as contemplated under Sections 106(A) and 108(A) of the NIRC of 1997, as amended.

However, the Court finds the deficiency VAT assessment on petitioner's gross rental income and proceeds from the sale of property and equipment to be in order.

Section 105 of the NIRC of 1997, as amended, provides as follows:

> "SEC. 105. *Persons Liable.* - Any person who, in the course of trade or business, sells, barters, exchanges, leases goods or properties, renders services, and any person who imports goods shall be subject to the value-added tax (VAT) imposed in Sections 106 and 108 of this Code.
>
> xxx xxx xxx
>
> The phrase 'in the course of trade or business' means the regular conduct or pursuit of a commercial or an economic activity, including transactions incidental thereto, by any person regardless of whether or not the person engaged therein is a nonstock, nonprofit private organization (irrespective of the disposition of its net income and whether or not it sells exclusively to members or their guests) or government entity."

Based on the foregoing, the VAT is imposed on a sale or transaction entered into by a person in the course of any trade or business. A transaction will be characterized as having been entered into by a person in the course of trade or business if it is (1) regularly conducted; and (2) undertaken in pursuit of a commercial or economic activity. Likewise, transactions that are made incidental to the pursuit of a commercial or economic activity are considered as entered into in the course of trade or business. "Incidental" means something else as primary; something necessary, appertaining to, or depending upon another, which is termed the principal. Hence, an isolated transaction is not necessarily disqualified from being made incidentally in the course of trade or business.[74]

Once an activity has been identified as a business, any supply (sale) made while carrying it on is likely to be made in the course or furtherance of business. No distinction is made between capital and revenue items. Thus, a supply (sale) in the course or furtherance of business includes: (1) the disposition of the assets and liabilities of a business; (2) the disposition of a business as going concern; and (3) anything done in connection with the termination or intended termination of a business.[75]

Absent such proof to the contrary, the sale of property and equipment subject of the assessment shall be considered to have been used by petitioner in the conduct of its business. Prior to the sale, the property and equipment formed part of petitioner's assets being used in its business operations. This means that petitioner's sale of property and equipment is an incidental transaction because the said property and equipment were used in furtherance of petitioner's business. Consequently, the proceeds from the sale in the amount of ₱317,400.00 shall be subject to 12% VAT imposed under Section 106(A) of the NIRC of 1997, as amended.

Similarly, petitioner's gross rental income in the amount of ₱1,621,815.83 shall be considered to have been made in the ordinary course of petitioner's trade or business. It is to be noted that petitioner is deemed to have conceded to the imposition of VAT on the said rental income as it did not make any objections thereto in its protest letter[76] dated February 20, 2008.

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[74] *CS Garments, Inc. vs. Commissioner of Internal Revenue*, CTA EB Case No. 287, January 17, 2008.
[75] *Ibid.*
[76] Exhibit "DD".

In view of the foregoing, petitioner is liable for basic deficiency VAT in the amount of ₱193,921.57, computed as follows:

Taxable Receipts per Return		₱ 80,112,975.20
Add: Gross Rental Income		1,621,815.83
Proceeds from Sale of Property and Equipment		317,400.00
Total VATable Receipts		₱ 82,052,191.03
Output Tax Due		₱ 8,205,219.10
Less: Input Tax per Audit		
Carry-over from Previous Quarter	₱ 334,851.26	
Input Tax from Goods and Services	7,654,608.49	
Total Available Input Tax	₱ 7,989,459.75	
Less: Carry-over to Succeeding Year	(294,520.97)	7,694,938.78
Net Output VAT Due		₱ 510,280.32
Less: Payment		316,358.75
Basic Deficiency VAT		**₱ 193,921.57**

E. DEFICIENCY DOCUMENTARY STAMP TAX - ₱338,695.26

According to respondent, petitioner's Rent Contracts with Saints Inc. Coffee Shop and Fort Bonifacio, Inc. in the respective amounts of ₱1,621,815.83 and ₱173,293,333.00 were not subjected to DST pursuant to Section 194 of the NIRC of 1997, as amended. These agreements have given rise to a deficiency DST liability in the amount of ₱338,695.26, inclusive of increments, computed as follows:

Rental Income (Saints Inc. Coffee Shop)	₱ 1,621,815.83	1st ₱2,000.00	₱ 3.00	
	1,619,815.83	₱1.00 Succeeding ₱1,000.00	1,620.00	₱ 1,623.00
Rental Expense (Fort Bonifacio)	₱173,293,333.00	1st ₱2,000.00	₱ 3.00	
	173,291,333.00	₱1.00 Succeeding ₱1,000.00	173,292.00	173,295.00
Basic Deficiency DST				₱ 174,918.00
Add: Penalties				
Surcharge				43,729.00

Interest (1/11/05 to 12/31/07)				104,048.26
Compromise				16,000.00
Total amount due and collectible				**₱338,695.26**

Petitioner counter-argues that respondent's three-year period to assess DST on a Contract of Lease which was executed between Fort Bonifacio Development Corporation and petitioner on August 3, 2001,[77] has already lapsed as provided under Section 203 of the NIRC of 1997, as amended. Further, respondent's assessment is invalid as it is based not on the lease agreement itself, but on other reports.

The Court partly sustains the deficiency DST assessment.

Respondent assessed petitioner for deficiency DST based on Section 194 of the NIRC of 1997, as amended, which reads:

> "SEC. 194. *Stamp Tax on Leases and Other Hiring Agreements.* - **On each lease**, agreement, memorandum, or contract for hire, use or rent **of any lands** or tenements, or portions thereof, **there shall be collected a documentary stamp tax of Three pesos (P3.00) for the first Two thousand pesos (P2,000)**, or fractional part thereof, **and an additional One peso (P1.00) for every One Thousand pesos (P1,000)** or fractional part thereof, **in excess of the first Two thousand pesos (P2,000) for each year of the term of said contract or agreement**." *(Emphasis supplied)*

In relation thereto, Section 200(B) of the NIRC of 1997, as amended, provides that the DST return shall be filed within ten (10) days after the close of the month when the taxable document was made, signed, issued, accepted, or

[77] Exhibit "SS".

transferred, and the tax thereon shall be paid at the same time the return is filed.

Applying the foregoing to the instant case, petitioner should have filed the DST return for the subject Contract of Lease and paid the corresponding DST to the BIR on September 10, 2001, at the latest, since the Contract of Lease between Fort Bonifacio Development Corporation and petitioner was executed on August 3, 2001. Clearly, petitioner's obligation to file the return and pay the corresponding DST liability already accrued on September 10, 2001.

Since the Contract of Lease with Fort Bonifacio Development Corporation pertains to petitioner's DST liability for the taxable year 2001, it was erroneous on the part of respondent to include the same as part of the deficiency DST assessment for the taxable year 2004. Thus, the basic deficiency DST of ₱173,295.00 assessed by respondent against petitioner on the Contract of Lease it executed with Fort Bonifacio Development Corporation on August 3, 2001 should be cancelled as it is outside the period covered by the assessment.

As regards the basic deficiency DST assessment of ₱1,623.00 pertaining to petitioner's Rent Contract with Saints Inc. Coffee Shop, petitioner is deemed to have admitted its deficiency DST liability because it did not contest the assessment.

F. IMPOSITION OF SURCHARGE, INTEREST AND COMPROMISE PENALTIES

The compromise penalties imposed by respondent cannot be sustained. Pursuant to Revenue Memorandum Order No. 01-90, compromise penalties are only amounts suggested in settlement of criminal liability, and may not be imposed or exacted on the taxpayer in the event that a taxpayer refuses to pay the same. Thus, compromise penalties imply a mutual agreement between the taxpayer and the Commissioner of Internal Revenue. Absent any showing that petitioner consented to the compromise penalties, the same should not be imposed.

As regards the interest and surcharge imposed by respondent against petitioner with respect to the deficiency income tax assessment for the taxable year 2004, this Court finds the same to be improper and therefore should be cancelled.

As held by the Supreme Court in the case of *Commissioner of Internal Revenue vs. St. Luke's Medical Center, Inc.*[78], to wit:

> "However, St. Luke's has good reasons to rely on the letter dated 6 June l990 by the BIR, which opined that St. Luke's is "a corporation for purely charitable and social welfare purposes" and thus exempt from income tax. In *Michael J Lhuillier, Inc. v. Commissioner of Internal Revenue,* the Court said that "good faith and honest belief that one is not subject to tax on the basis of previous interpretation of government agencies tasked to implement the tax law, are sufficient justification to delete the imposition of surcharges and interest."

However, this Court finds petitioner liable to the interest and surcharge related to its deficiency EWT, WTC, VAT and DST liabilities for the taxable year 2004.

WHEREFORE, premises considered, the instant consolidated Petitions for Review are hereby **PARTIALLY GRANTED**.

The assessment issued by respondent against petitioner for the taxable year **2003** covering alleged

[78] *Supra.*

deficiency income tax for the taxable year 2003 is hereby **CANCELLED** due to prescription.

However, the assessments issued by respondent against petitioner for the taxable year **2004** covering deficiency income tax, deficiency value-added tax, deficiency withholding tax on compensation, deficiency expanded withholding tax and deficiency documentary stamp tax are **UPHELD** but with some modifications.

Accordingly, petitioner is hereby **ORDERED TO PAY** the amount of **₱151,850,822.97** for the following deficiency taxes, inclusive of the 25% surcharge imposed under Section 248(A)(3) of the NIRC of 1997, as amended:

Type of Tax	Basic Tax	25% Surcharge	Total
Income Tax	₱ 132,011,615.87		₱ 132,011,615.87
Value-added Tax	193,921.57	₱ 48,480.39	242,401.96
Withholding Tax on Compensation	2,317,996.65	579,499.16	2,897,495.81
Expanded Withholding Tax	13,357,824.46	3,339,456.12	16,697,280.58
Documentary Stamp Tax	1,623.00	405.75	2,028.75
	₱147,882,981.55	**₱3,967,841.42**	**₱151,850,822.97**

In addition, petitioner is hereby **ORDERED TO PAY** 20% deficiency interest per annum on the following basic deficiency taxes computed from the dates indicated herein after full payment thereof pursuant to Section 249(B) of the NIRC of 1997, as amended:

	Basic Deficiency Tax	Computed from:
Value-added Tax	₱ 193,921.57	January 25, 2005
Withholding Tax on Compensation	2,317,996.65	January 15, 2005
Expanded Withholding Tax	13,357,824.46	January 15, 2005
Documentary Stamp Tax	1,623.00	January 10, 2005
	₱ 15,871,365.68	

Further, petitioner is hereby **ORDERED TO PAY** 20% delinquency interest per annum on the deficiency taxes of ₱15,871,365.68, on the 25% surcharge of ₱3,967,841.42 and on the 20% deficiency interest which have accrued as stated above from December 31, 2007 until full payment.

thereof pursuant to Section 249(C) of the NIRC of 1997, as amended.

SO ORDERED.

Cielito N. Mindaro-Grulla
CIELITO N. MINDARO-GRULLA
Associate Justice

WE CONCUR:

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Associate Justice

CAESAR A. CASANOVA
Associate Justice

ATTESTATION

I attest that the conclusions in the above Decision were reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Associate Justice
Chairperson

CERTIFICATION

Pursuant to Article VIII, Section 13 of the Constitution, and the Division Chairperson's Attestation, it is hereby certified that the conclusions in the above Decision were reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

ROMAN G. DEL ROSARIO
Presiding Justice