

REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

Special Third Division

**PERPETUAL SUCCOUR
HOSPITAL OF CEBU,
INC.,**

CTA Case No. 9166

Petitioner,

-versus-

**COMMISSIONER OF
INTERNAL REVENUE,**
Respondents.

Members:
FABON-VICTORINO, *Acting*
Chairperson, and
RINGPIS-LIBAN, JJ.

Promulgated:

DEC 11 2018

1:56 p.m.

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DECISION

RINGPIS-LIBAN, J.:

Before us is a Petition for Review filed on October 6, 2015 by Perpetual Succour Hospital of Cebu, Inc., praying for the annulment of the Final Decision issued by the Commissioner of Internal Revenue that found it liable for alleged deficiency income tax for taxable year 2010 in the total amount of ₱19,912,123.87.

THE FACTS

Petitioner Perpetual Succour Hospital of Cebu, Inc. (PSHCI) is incorporated as a religious, non-stock, non-profit, charitable institution governed by a Board of Trustees, owned by the Congregation of the Sisters of St. Paul De Chartres (SPC). Its registered address is at Gorordo Avenue, Camputhaw, Cebu City.¹

¹ Exhibit "P-8-A", docket, p. 116.

On the other hand, respondent is the duly appointed Commissioner of the Bureau of Internal Revenue (BIR) who has the power to decide disputed assessments, refunds of internal revenue taxes, fees or other charges, penalties imposed in relation thereto or other matters arising under the National Internal Revenue Code (NIRC) or other laws or portions thereof administered by the BIR. He holds office at the BIR National Office Building, Agham Road, Diliman, Quezon City.

A Preliminary Assessment Notice² (PAN) dated February 17, 2015 was issued against petitioner, assessing and demanding payment from petitioner of the amount of ₱156,153,345.45 for alleged income tax, value-added tax, and expanded withholding tax deficiencies for taxable year 2010. Petitioner protested the PAN in a letter mailed on March 4, 2015³.

In the Formal Letter of Demand (FLD) and Final Assessment Notice (FAN) dated March 23, 2015, petitioner's protest was denied and petitioner was given a demand for payment of ₱141,056,012.24 as deficiency income tax.⁴ In turn, petitioner filed a protest letter on April 14, 2015⁵.

In the Final Decision on Disputed Assessment⁶ (FDDA) dated May 21, 2015, petitioner's protest was denied and it was demanded to pay deficiency income tax in the amount of ₱143,686,399.62. Petitioner then filed a motion for reconsideration with respondent.⁷

Subsequently, respondent issued a Final Decision⁸ that reduced the amount of deficiency income tax to ₱19,912,123.87. The Final Decision was received by petitioner on September 7, 2015.

As a result, petitioner filed the instant Petition for Review on October 6, 2015.⁹

Respondent then filed his Answer¹⁰ on December 10, 2015, interposing the following special and affirmative defenses:

² Exhibit "R-8", BIR Records, pp. 680-688.

³ Exhibit "R-11", BIR Records, p. 796.

⁴ Exhibits "R-10" and "R-11", BIR Records, pp. 791-796.

⁵ Exhibit "R-13", BIR Records, p. 830.

⁶ Exhibit "R-13", BIR Records, pp. 826-830.

⁷ Exhibit "R-14", BIR Records, p. 866.

⁸ Exhibit "R-14", BIR Records, pp. 865-866.

⁹ Docket, pp. 11-18.

¹⁰ Docket, pp. 49-57.

**“THE TAX ASSESSMENT IS
NOT BARRED BY RES JUDICATA.**

5. Petitioner contends that its exemption from income tax has long been honored per BIR Rulings then firmly affirmed by the Honorable Court in CTA Case No. 7304, by the Honorable Court En Banc in CTA EB Case No. 781 and by the Honorable Supreme Court in G.R. No. 201905 which have become final and executory. It is therefore the controlling jurisprudence between petitioner and respondent.

6. Petitioner further invoked the doctrine on conclusiveness of judgment and that a ruling in a prior assessment bars petitioner from being subject of a new assessment.

7. Petitioner’s contention is specious. Respondent strongly interposes that res judicata cannot be made applicable to the case at hand.

8. The Honorable Supreme Court in the case of *Digital Telecommunications vs. Jessie Cantos* made it explicit:

Res judicata means a matter adjudged; a thing judicially acted upon or decided; a thing or matter settled by judgment. For res judicata to apply there must among others be, between the first and the second actions, identity of the parties, identity of subject matter, and identity of causes of action.

9. There might be identity of the parties between the previous case and the case at hand, but the subject matter and the cause of action are dissimilar. Careful perusal of the decision of the Honorable Court under CTA Case No. 7304 reveals that it involves an assessment for income tax for the taxable year 2001. The assessment subject of the instant petition is that of taxable year 2010.

10. Respondent further submits that the factual background surrounding the two taxable years are different and if considered will warrant petitioner’s liability for income tax for taxable year 2010.



11. Foregoing considered, respondent is not barred from issuing the assessment for the taxable year 2010.

**TAX EXEMPTION ARE
CONSTRUED STRICTISSIMI JURIS.
HENCE, AN ESSENTIAL
REQUISITE FOR EXEMPTION
MUST BE CONTINUOUSLY
PROCESSED.**

12. Petitioner submits that being a nonstock corporation, it is exempt from income tax pursuant to Section 30(E) of the National Internal Revenue Code which provides:

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13. Petitioner further argued that its status being exempt from income tax was already judicially ruled by the Honorable Court in CTA Case No. 7304. Hence, its tax exemption cannot be disturbed directly or indirectly.

14. With all due respect to the Honorable Court, respondent strongly differs. Tax exemption are construed *strictissimi juris*. The requirements provided for by law for tax exemption must be continually satisfied by the taxpayer in order to enjoy immunity from taxation. Therefore, respondent is not precluded from conducting an investigation in order to insure that the taxpayer continuously meets the criteria for exemption for each taxable year.

15. In the Formal Letter of Demand dated 23 March 2015, respondent, through Assistant Commissioner Nestor S. Valeroso, found that petitioner has not fully complied with the exclusivity and inurement provisions of Section 30(E) for it to be exempt from tax. RMO 51-2015 dated June 11, 2014 further clarifies the inurement prohibition under Section 30(E). A part of the RMC reads:

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Therefore, in order for an entity to qualify as a non-stock and/or non-profit corporation/association/organization exempt from Income Tax under Section 30 of the NIRC, as amended, its earnings or assets shall not inure to the benefit of any of its trustees, organizers, officers, members or any specific person.



The following are considered 'inurement' of such nature:

1. The payment of compensation, salaries, or honorarium to its trustees or organizers;
2. The payment of exorbitant or unreasonable compensation to its employees;
3. The provision of welfare aid and financial assistance to its members xxx
4. xxx

RMC 07-2012 dated October 31, 2012:

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 operation of the charitable organization must be devoted 'exclusively' for charitable purposes.
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16. Upon audit, petitioner's records showed that it was run by the Congregation of the Sisters of Saint Paul de Chartres and is not operated exclusively for charitable purposes. Petitioner's General Ledger for CY 2010 showed that Charities and Discounts accounts totaling P73.1 Million is only 8.3% of its total revenues of P876.7 Million.

17. Petitioner's records also showed that it was regularly supporting the congregation of the Sisters of St. Paul of Chartres which according to its Amended By-Laws, Sec. 1 is a member of the corporation thus disproving its claim that no amount inures directly or indirectly to its officers, employees, or members. General Ledger entries/records of its support to the congregation totaled P7.8 Million during the year under audit, viz:



	Acct. Code	Acct. Description	Amount
2010	670-430	Religious Support	4,287,200.00
2010	670-465	Support for Community Sisters	784,535.76
2010	670-449	Support to SPC Provinciabile	1,807,119.00
2010	670-468	Foods, Mdg. & Subs (Sisters)	966,188.13
			7,845,042.89

18. Thus, petitioner is subject to the preferential tax rate of 10% under Sec. 27(B) of the NIRC since both provisions under Sec. 30(E) were not met upon actual audit of its books, viz:

- a.) The provisions of being operated exclusively for charitable purpose;
- b.) The provisions of inurement or welfare aid and financial assistance to members of the organization or association.

19. Based on the audit findings of respondent's Large Taxpayers Service, petitioner failed to comply with the requirements provided by law 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.

20. Further, in the Honorable Court's decision in CTA Case No. 7304 involving an assessment on petitioner for the taxable year 2001, it provided

'As testified by petitioner's witness, Sister Maria Lirio Gavan, any income received by petitioner is devoted and plowed back to charity and no part of thereof goes for the personal gain or inures to the benefit of the SPC Congregation or its members. Also, on direct examination, Sister Zeta Caridad Rivero testified that no income or part thereof is used for personal gain by any of the SPC members.

Likewise, there is no evidence on record that will show that other persons, natural or juridical, other than the beneficiaries of petitioner's charitable activities, have benefited directly or indirectly from petitioner's assets or income.' (Emphasis ours)

21. Respondent strongly submits that results of the investigation conducted reveal that the factual background surrounding the cited case are different from the case at hand. As



discussed extensively above, petitioner failed to comply with the requirement that no part of its net income or asset shall inure to the benefit of any member, organizer, officer, or any specific person. Thus, petitioner cannot therefore raise a defense of immunity from income tax to avoid its liabilities.

**THE TAX ASSESSMENT WERE ISSUED IN
ACCORDANCE WITH LAW, RULES AND
JURISPRUDENCE.**

22. The audit investigation conducted against petitioner was in accordance with law and jurisprudence and afforded petitioner due process.

23. From an initial finding of ₱156,153,345.45 in the Preliminary Assessment Notice, the tax liability was finally reduced to only ₱19,912,123.87. Thus, in the FDDA, it was stated that:

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24. As can be deduced from the following narrations of facts, the procedure prescribed under Revenue Regulations No. 12-99 had been complied with by respondent.

25. Based on the foregoing, the finding of deficiency tax liabilities against petitioner for taxable year 2010 is proper in all respects. xxx”

The case was subsequently set for pre-trial conference on March 15, 2016.¹¹ Accordingly, respondent’s Pre-Trial Brief¹² was filed on March 10, 2016; while petitioner’s Pre-Trial Brief¹³ was filed on March 15, 2016.

The parties filed their Joint Stipulation of Facts and Issues¹⁴ on April 29, 2016. Thereafter, a Pre-Trial Order¹⁵ was issued by the Court on May 16, 2016.

Trial ensued, giving both parties the opportunity to present their respective documentary and testimonial evidence.



¹¹ Docket, p. 59.

¹² Docket, pp. 88-92.

¹³ Docket, pp. 97-101.

¹⁴ Docket, pp. 198-202.

¹⁵ Docket, pp. 205-209.

After presentation, marking, identification, and offer, the Court admitted Exhibits “P-1”, “P-2” to “P-26”, “P-8-A”, “P-35”, and “35-a” as part of petitioner’s documentary evidence; while Exhibits “P-27”, “P-28”, “P-29”, “P-30”, “P-31”, “P-32”, “P-33”, and “34” were denied admission.¹⁶

On the other hand, the Court admitted Exhibits “R-1” to “R-15-a” as part of respondent’s evidence.¹⁷

The Court declared the case submitted for decision on December 20, 2017,¹⁸ considering petitioner’s Memorandum¹⁹ filed on December 6, 2017 and the Records Verification Report²⁰ issued by the Court’s Judicial Records Division stating that respondent failed to file his Memorandum.

THE ISSUES

The parties submitted the following issues for this Court’s disposition:²¹

1. Whether petitioner possesses all the qualification to be exempt from income tax under Section 30 of the NIRC of 1997?
2. Whether or not respondent is correct in assessing petitioner for deficiency income tax in the aggregate amount of ₱19,912,123.87 for taxable year 2010 plus 25% surcharge and 20% deficiency and delinquency interests for late payment pursuant to Sections 248 and 249 of the NIRC of 1997?

THE RULING OF THE COURT

Before proceeding to the stipulated issues, the Court shall first determine the timeliness of the filing of this Petition for Review.

Section 228 of the National Internal Revenue Code of 1997, as amended, provides:

“SEC. 228. *Protesting of Assessment.* – When the Commissioner or his duly authorized representative finds that

¹⁶ Resolution dated February 3, 2017, docket, pp. 235-236.

¹⁷ Resolution dated October 11, 2017, docket, pp. 288-289.

¹⁸ Resolution, docket, p. 309.

¹⁹ Docket, pp. 290-304.

²⁰ Docket, p. 307.

²¹ Stipulation of Issues, Joint Stipulation of Facts and Issues, docket, p. 199.

proper taxes should be assessed, he shall first notify the taxpayer of his findings: *Provided, however,* That a preassessment notice shall not be required in the following cases:

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The taxpayers shall be informed in writing of the law and the facts on which the assessment is made; otherwise, the assessment shall be void.

Within a period to be prescribed by implementing rules and regulations, the taxpayer shall be required to respond to said notice. If the taxpayer fails to respond, the Commissioner or his duly authorized representative shall issue an assessment based on his findings.

Such assessment may be protested administratively by filing a request for reconsideration or reinvestigation within thirty (30) days from receipt of the assessment in such form and manner as may be prescribed by implementing rules and regulations. Within sixty (60) days from filing of the protest, all relevant supporting documents shall have been submitted; otherwise, the assessment shall become final.

If the protest is denied in whole or in part, or is not acted upon within one hundred eighty (180) days from submission of documents, the taxpayer adversely affected by the decision or inaction may appeal to the Court of Tax Appeals within thirty (30) days from receipt of the said decision, or from the lapse of the one hundred eighty (180)-day period; otherwise, the decision shall become final, executory and demandable.”

Based on the foregoing, since petitioner received the copy of respondent’s Final Decision²² on September 7, 2015, petitioner had 30 days or until October 7, 2015 within which to file an appeal before this Court. Consequently, the Petition for Review was timely filed on October 6, 2015.

The Court shall now proceed to determine whether petitioner is liable for the assessed deficiency income tax and interest.

Petitioner claims that this Court has already ruled in CTA Case No. 7304 that petitioner possesses the qualifications to be exempt from income tax under Section 30(E) of the NIRC of 1997, as amended, since it is not organized for

²² Exhibit “R-14”, BIR Records, pp. 865-866.

profit, it has no capital stock divided into shares, it is a non-profit corporation and it is a charitable institution; thus, Section 27(B) of the same Code, which provides for a preferential rate of ten percent (10%) for income tax, is not the applicable provision.

According to petitioner, no part of its income inure to SPC members, or any person. Being in compliance with the requisites of Section 30(E) of the NIRC of 1997, as amended, no tax on income is due, thus, a finding of “deficiency” is unlikely.

Respondent opposes the above arguments, alleging that the subject assessment is not barred by the Court’s earlier ruling in *Perpetual Succour Hospital, Inc. and the Sisters of St. Paul de Charters vs. Commissioner of Internal Revenue*, CTA Case No. 7304, December 1, 2010.

Respondent adds that tax exemptions are construed *strictissimi juris*. Hence, the essential requisites for exemption must be continuously possessed in order to be exempt from taxation.

As to the allegation that the doctrine of conclusiveness of judgment is applicable in this case, the Court finds the same bereft of merit.

In *Perpetual Succour Hospital, Inc. and the Sisters of St. Paul de Charters vs. Commissioner of Internal Revenue*²³, CTA Case No. 7304, the Court held that petitioner is a non-stock, non-profit, religious and charitable institution.

The above decision was appealed before the Supreme Court docketed as G.R. No. 201905 and was later dismissed in a minute resolution because the High Court found no ground to warrant the reversal of the said decision.

Petitioner thus submits that the above findings bar respondent from assessing it for deficiency income tax based on the doctrine of conclusiveness of judgment.

In the case of *Social Security Commission vs. Rizal Poultry and Livestock Association, Inc., et al.*²⁴, the Supreme Court explained the concept of *res judicata* known as “conclusiveness of judgment” as follows:

“But where there is identity of parties in the first and second cases, but no identity of causes of action, **the first judgment is conclusive only as to those matters actually and**

²³ Promulgated on December 1, 2010.

²⁴ G.R. No. 167050, June 1, 2011.

directly controverted and determined and not as to matters merely involved therein. This is the concept of *res judicata* known as ‘conclusiveness of judgment.’ Stated differently, **any right, fact or matter in issue directly adjudicated or necessarily involved in the determination of an action before a competent court in which judgment is rendered on the merits is conclusively settled by the judgment therein and cannot again be litigated between the parties and their privies, whether or not the claim, demand, purpose, or subject matter of the two actions is the same.”** (*Emphasis supplied*)

Based on the foregoing, in case there is identity of parties in the first and second cases, but no identity of causes of action, the first judgment is conclusive only as to those matters actually and directly controverted and determined and not as to matters merely involved therein.

Applying the afore-cited Supreme Court ruling, this Court finds CTA Case No. 7304 inapplicable to the present case inasmuch as the evidence presented therein was not directly controverted. In fact, the Former Second Division of the CTA categorically stated in its ruling that “respondent [CIR] failed to controvert” the evidence presented by petitioner that it is “a non-stock, non-profit, religious and charitable institution.” Thus, the judgment thereon cannot be considered as a conclusively settled fact or question.

Aside from the fact that the instant case involves petitioner’s income for taxable year 2010, the findings of respondent as provided in the Details of Discrepancies in the FLD showed that petitioner supports SPC, which according to its Amended By-Laws, is a member of the corporation, thus, disproving its claim that no amount inures directly or indirectly to petitioner’s officers, employees or members. General Ledger entries/record of its support to the congregation amounted to ₱7.8 million during the year.

These matters were not considered in the previous decision of this Court in CTA Case No. 7304, which was later affirmed in CTA EB No. 781 and, on appeal, affirmed by the Supreme Court in G.R. No. 201905, as the same only involves transactions made for taxable year 2001.

In view of the foregoing, the Court finds that the doctrine of conclusiveness of judgment does not apply in this case.

Equally noteworthy is the fact that the ruling of the Supreme Court in G.R. No. 201905 is merely in a form of a minute resolution, which is not considered a binding precedent.



In the case of *Deutsche Bank AG Manila Branch vs. Commissioner of Internal Revenue*²⁵, the Supreme Court explained the effect of a minute resolution in this wise:

“At the outset, this Court’s minute resolution on *Mirant* is not a binding precedent. The Court has clarified this matter in *Philippine Health Care Providers, Inc. v. Commissioner of Internal Revenue* as follows:

It is true that, although contained in a minute resolution, our dismissal of the petition was a disposition of the merits of the case. When we dismissed the petition, we effectively affirmed the CA ruling being questioned. As a result, our ruling in that case has already become final. When a minute resolution denies or dismisses a petition for failure to comply with formal and substantive requirements, the challenged decision, together with its findings of fact and legal conclusions, are deemed sustained. But what is its effect on other cases?

With respect to the same subject matter and the same issues concerning the same parties, it constitutes *res judicata*. However, if other parties or another subject matter (even with the same parties and issues) is involved, the minute resolution is not binding precedent. Thus, in *CIR v. Baier-Nickel*, the Court noted that a previous case, *CIR v. Baier-Nickel* involving the same parties and the same issues, was previously disposed of by the Court thru a minute resolution dated February 17, 2003 sustaining the ruling of the CA. Nonetheless, the Court ruled that the previous case ‘ha(d) no bearing’ on the latter case because the two cases involved different subject matters as they were concerned with the taxable income of different taxable years.

Besides, there are substantial, not simply formal, distinctions between a minute resolution and a decision. The constitutional requirement under the first paragraph of Section 14, Article VIII of the Constitution that the facts and the law on which the judgment is based must be expressed clearly and distinctly applies only to decisions, not to minute

²⁵ G.R. No. 188550, August 19, 2013, citing *Philippine Health Care Providers, Inc. vs. Commissioner of Internal Revenue*, G.R. No. 167330, September 18, 2009.

resolutions. A minute resolution is signed only by the clerk of court by authority of the justices, unlike a decision. It does not require the certification of the Chief Justice. Moreover, unlike decisions, minute resolutions are not published in the Philippine Reports. Finally, the *proviso* of Section 4(3) of Article VIII speaks of a decision. Indeed, as a rule, this Court lays down doctrines or principles of law which constitute binding precedent in a decision duly signed by the members of the Court and certified by the Chief Justice. (Emphasis supplied)

Even if we had affirmed the CTA in *Mirant*, the doctrine laid down in that Decision cannot bind this Court in cases of a similar nature. There are differences in parties, taxes, taxable periods, and treaties involved; more importantly, the disposition of that case was made only through a minute resolution.”

Clearly, the fact that the Court of Tax Appeals ruled in the previous case that petitioner is exempt from payment of income tax for taxable year 2001, which was affirmed by the Supreme Court in a minute resolution, does not make it a binding precedent in determining petitioner’s exemption from income tax for taxable year 2010.

Considering the foregoing, the Court shall now address the issue pertaining to petitioner’s alleged exemption from payment of the 10% preferential rate of income tax for taxable year 2010.

In the appealed Final Decision, respondent found petitioner liable to pay the reduced deficiency income tax in the amount of ₱19,912,123.87, applying the 10% preferential tax rate under Section 27(B) of the NIRC of 1997, as amended, which reads as follows:²⁶

“SEC. 27. *Rates of Income Tax on Domestic Corporations.* –

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(B) *Proprietary Educational Institutions and Hospitals.* – Proprietary educational institutions and hospitals which are non-profit 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

²⁶ Exhibit “R-14”, BIR Records, pp. 865-866.

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.”

The assessment in the said decision was in response to petitioner’s request for reconsideration filed with the Office of the Commissioner of Internal Revenue, after the issuance of the FDDA by the OIC – Assistant Commissioner of the Large Taxpayers Services of the Bureau of Internal Revenue. The FDDA found that SPC was the organizer of petitioner. Since petitioner is regularly contributing to the operations of SPC, then part of its asset benefited the congregation.

Petitioner presented the testimony of Sister Zeta Rivero, petitioner’s Administrator, to prove that no funds of petitioner inured directly to the benefit of the SPC nuns.²⁷

On cross-examination, Sister Zeta Rivero testified that petitioner remits funds to SPC. Associate Justice Ma. Belen M. Ringpis-Liban propounded clarificatory questions, wherein Sister Zeta Rivero answered that the remittance was for the support of SPC’s old sisters, for their religious missions of taking care of the poor and sick, and for education. In response to the question of Associate Justice Esperanza R. Fabon-Victorino, Sister Zeta Rivero explained that the funds remitted to SPC is called support of religious and that such is not equivalent to a salary.²⁸

Petitioner invokes Section 30(E) of the NIRC of 1997, as amended, claiming that it is exempt from payment of the 10% income tax provided in Section 27(B) of the NIRC of 1997, as amended.

Under Section 30(E) of the NIRC of 1997, as amended, one of the requirements for a charitable institution to be exempt from income tax is that no

²⁷ Exhibits “P-35”, docket, pp. 106-108.

²⁸ Transcript of Stenographic Notes taken on November 15, 2016, pp. 8-12.

part of its net income or asset shall belong to or inure to the benefit of any member, organizer, officer or any specific person, to wit:

“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:

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

The application of Section 27(B) in relation to Section 30(E) of the NIRC of 1997, as amended, was extensively discussed by the Supreme Court in the case of *Commissioner of Internal Revenue vs. St. Luke's Medical Center, Inc.*²⁹, the significant parts of which are quoted hereunder:

“xxx We hold that Section 27(B) of the NIRC does not remove the income tax exemption of proprietary non-profit 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**

²⁹ G.R. Nos. 195909 and 195960, September 26, 2012.



devoted to the institution's purposes and all its activities conducted not for profit.

'Non-profit' does not necessarily mean 'charitable.' In *Collector of Internal Revenue v. Club Filipino, Inc. de Cebu*, this Court considered as non-profit a sports club organized for recreation and entertainment of its stockholders and members. The club was primarily funded by membership fees and dues. If it had profits, they were used for overhead expenses and improving its golf course. The club was non-profit because of its purpose and there was no evidence that it was engaged in a profit-making enterprise.

The sports club in *Club Filipino, Inc. de Cebu* may be non-profit, but it was not charitable. The Court defined 'charity' in *Lung Center of the Philippines v. Quezon City* 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 [by] **otherwise lessening the burden of government.**' A non-profit club for the benefit of its members fails this test. An organization may be considered as non-profit if it does not distribute any part of its income to stockholders or members. However, despite its being a tax exempt institution, any income such institution earns from activities conducted for profit is taxable, as expressly provided in the last paragraph of Section 30.

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Charitable institutions, however, are not *ipso facto* entitled to a tax exemption. The requirements for a tax exemption are specified by the law granting it. The power of Congress to tax implies the power to exempt from tax. Congress can create tax exemptions, subject to the constitutional provision that '[n]o law granting any tax exemption shall be passed without the concurrence of a majority of all the Members of Congress.' The requirements for a tax exemption are strictly construed against the taxpayer because an exemption restricts the collection of taxes necessary for the existence of the government.

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As a general principle, a charitable institution does not lose its character as such and its exemption from taxes simply because it derives income from



paying patients, whether out-patient, 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.

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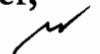
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Section 30(E) of the NIRC provides that a charitable institution must be:

- (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.”
(*Emphasis supplied*)

Section 30(E) of the NIRC of 1997, as amended, clearly requires that “no net income or asset accrues to or benefits any member or specific person”.

In this case, the evidence of petitioner shows that the contribution inured to the benefit of SPC because, as testified to by petitioner’s witness, the funds were used to support the activities of SPC.

However, there is nothing from respondent’s findings which would show that the said contribution belong to or inure to the benefit of the members of the board of trustees in their individual capacity.

As held in the above case, Section 30(E) of the NIRC of 1997, as amended, provides that a charitable institution must likewise be operated exclusively for charitable purposes for the exemption to apply.

In the subject Final Decision, respondent applied the preferential rate of 10% under Section 27(B) of the NIRC of 1997, as amended, on revenues from services to paying patients instead of exempting petitioner from income tax as provided under Section 30(E) of the same Code.

In the same *Commissioner of Internal Revenue vs. St. Luke’s Medical Center, Inc.*³⁰ case, the Supreme Court further held as follows:

“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

³⁰ G.R. Nos. 195909 and 195960, September 26, 2012.

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%.

In 1998, St. Luke's had total revenues of **₱1,730,367,965** from services to paying patients. It cannot be disputed that a hospital which receives approximately **₱1.73** 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.' Indeed, St. Luke's admits that it derived profits from its paying patients. St. Luke's declared **₱1,730,367,965** as 'Revenues from Services to Patients' in contrast to its 'Free Services' expenditure of **₱218,187,498**. In its Comment in G.R. No. 195909, St. Luke's showed the following 'calculation' to support its claim that 65.20% of its 'income after expenses was allocated to free or charitable services' in 1998.

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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 ₱1.73 billion total revenues from paying patients is not even incidental to St. Luke's charity expenditure of ₱218,187,498 for non-paying patients.

St. Luke's claims that its charity expenditure of **₱218,187,498** 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.'

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The question was whether having a hospital is essential to an educational institution like the College of Medicine of the University of Santo Tomas. Senator Cuenco answered that if the hospital has paid rooms generally occupied by people of good economic standing, then it should be subject to income tax. He said that this was one of the reasons Congress inserted the phrase 'or any activity conducted for profit.'

The question in *Jesus Sacred Heart College* involves an educational institution. However, it is applicable to charitable institutions because Senator Cuenco's response shows an intent to focus on the activities of charitable institutions. **Activities for profit should not escape the reach of taxation. Being a non-stock and non-profit corporation does not, by this reason alone, completely exempt an institution from tax. An institution cannot use its corporate form to prevent its profitable activities from being taxed.**

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. 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. **An 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).**

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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."
(Emphasis supplied)



The Supreme Court in the above case clearly stated that 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. However, 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”.

It is true that petitioner was previously held to be an institution under Section 30(E) of the NIRC of 1997, as amended, which does not lose its tax exemption if it earns income from its for-profit activities. However, applying the above ruling, such income from for-profit activities, under the last paragraph of Section 30, shall be subject to income tax, at the preferential 10% tax rate under Section 27(B) of the NIRC of 1997, as amended.

Thus, the Court sustains the imposition of the 10% preferential tax rate under Section 27(B) of the NIRC of 1997, because petitioner failed to controvert by evidence respondent’s finding that petitioner is not “operated exclusively for charitable purpose” for taxable year 2010.

It must be emphasized that taxation is the rule and exemption is the exception. The burden of proof rests upon the party claiming exemption to prove that it is, in fact, covered by the exemption so claimed.³¹ In this case, petitioner failed to prove that it is exempt from the 10% income tax provided under Section 27(B) of the NIRC of 1997, as amended. Thus, respondent’s findings of deficiency income tax in the appealed Final Decision shall prevail.

However, following the Supreme Court’s ruling in *Commissioner of Internal Revenue vs. St. Luke’s Medical Center, Inc.*³², petitioner is not liable to pay interest and compromise penalty, thus:

“As to whether SLMC is liable for compromise penalty under Section 248(A) of the 1997 NIRC for its alleged failure to file its quarterly income tax returns, this has also been resolved in G.R. Nos. 195909 and 195960 (*Commissioner of Internal Revenue v. St. Luke’s Medical Center, Inc.*), where the imposition of surcharges and interest under Sections 248 and 249 of the 1997 NIRC were deleted on the basis of good faith and honest belief on the part of SLMC that it is not subject to tax. Thus, following the ruling of the Court in the said case, SLMC is not liable to pay compromise penalty under Section 248(A) of the 1997 NIRC.”



³¹ Philippine Amusement and Gaming Corporation (PAGCOR) vs. The Bureau of Internal Revenue, G.R. No. 172087, March 15, 2011.

³² G.R. No. 203514, February 13, 2017.

In this case, petitioner appears to have honestly believed in good faith that it is not liable to pay the assessed tax because of the previous findings of this Court in CTA Case No. 7304. Hence, the interest and the compromise penalty shall likewise be deleted on the basis of good faith and honest belief on the part of petitioner that it is not subject to tax.

WHEREFORE, premises considered, the instant Petition for Review is **PARTIALLY GRANTED**. The decision of the Commissioner of Internal Revenue insofar as it holds petitioner liable for basic deficiency income tax is **UPHELD**, while the assessed interest and compromise penalty amounting to ₱9,272,472.67 and ₱50,000.00, respectively, are **CANCELLED**. Accordingly, petitioner is **ORDERED TO PAY** the basic deficiency income tax for taxable year 2010 in the amount of ₱10,589,651.20.

SO ORDERED.

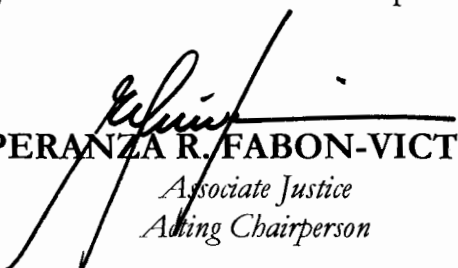

MA. BELEN M. RINGPIS-LIBAN
Associate Justice

I CONCUR:


ESPERANZA R. FABON-VICTORINO
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.


ESPERANZA R. FABON-VICTORINO
Associate Justice
Acting Chairperson

CERTIFICATION

Pursuant to Section 13 of Article VIII of the Constitution, and the Acting 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.

A handwritten signature in black ink, appearing to read 'Roman G. Del Rosario', with a stylized, cursive script.

ROMAN G. DEL ROSARIO

Presiding Justice