REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

EN BANC

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

- versus -

PERPETUAL SUCCOUR HOSPITAL OF CEBU, INC.,
Respondent.

CTA EB NO. 1819
(CTA Case No. 8912)

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PERPETUAL SUCCOUR HOSPITAL OF CEBU, INC.,
Petitioner,

- versus -

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

CTA EB NO. 1841
(CTA Case No. 8912)

Present:

DEL ROSARIO, *PJ;*
CASTAÑEDA, JR.,
UY,
FABON-VICTORINO,
MINDARO-GRULLA,
RINGPIS-LIBAN,
MANAHAN,
BACORRO-VILLENA, and
MODESTO-SAN PEDRO, *JJ.*

Promulgated:

OCT 10 2019

10:52 a.m.

x - x

DECISION

Fabon-Victorino, J.:

In these consolidated Petitions for Review, the Commissioner of Internal Revenue (CIR) and Perpetual Succour Hospital of Cebu, Inc. (PSH) assail the Decision[1]

[1] Court in Division docket, pp. 530-560.

and Resolution[2] respectively dated July 25, 2017 and March 13, 2018, rendered by the Court in Division in CTA Case No. 8912, entitled *Perpetual Succour Hospital of Cebu, Inc. vs. Commissioner of Internal Revenue*. The dispositive portion of the assailed Decision and Resolution read as follows:

Assailed Decision of July 25, 2017:

> **WHEREFORE**, premises considered, the instant Petition for Review is **PARTIALLY GRANTED.** Accordingly, the decision of the Commissioner of Internal Revenue appealed from, insofar as it holds petitioner liable for basic deficiency income tax is **UPHELD** and petitioner is **ORDERED** to **PAY** the basic deficiency income tax in the amount of P8,179,619.66, while the assessed interest and compromise penalty amounting to P7,329,848.06 and P25,000.00, respectively, are hereby **CANCELLED**.
>
> **SO ORDERED.**

Assailed Resolution of March 13, 2018:

> **WHEREFORE**, premises considered, respondent's Motion for Partial Reconsideration and petitioner's Motion for Reconsideration are both **DENIED** for lack of merit.
>
> **SO ORDERED.**

In his *Petition for Review*[3] filed on April 13, 2018, docketed as CTA EB No. 1819, the CIR prays that the assailed Decision and Resolution be partially reversed and set aside; and that in addition to the basic deficiency income tax (IT), PSH be ordered to also pay compromise penalty, deficiency and delinquency interests pursuant to Sections 248 and 249 of the National Internal Revenue Code (NIRC) of 1997, as amended.

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[2] Court in Division docket, pp. 650-655.
[3] *En Banc* docket (CTA EB No. 1819), pp. 7-21.

On the other hand, PSH, in its *Petition for Review*[4] filed on May 10, 2018, and docketed as CTA EB No. 1841, prays that the assailed Decision and Resolution be reversed and set aside, and that a new one be issued cancelling the assessed deficiency income tax in the amount of Php8,179,619.66.

The Established Facts and the Proceedings

PSH is a non-stock, non-profit, religious and charitable institution operating a hospital at Gorordo Avenue, Lahug, Cebu City.

The CIR, on the other hand, represents the Bureau of Internal Revenue (BIR) as its head with address at BIR National Office Building, Agham Road, Diliman, Quezon City.

PSH and St. Paul De Chartres (SPC) and the CIR were the parties in CTA Case No. 7304, in which PSH questioned before the Court in Division the assessment for deficiency income tax (IT) for taxable year (TY) 2001 issued against it by the CIR. In its Decision dated December 1, 2010, the Court's Former Second Division held that PSH is a non-profit corporation, operated exclusively for religious and charitable purpose and, thus, fall under Section 30(E) of the NIRC of 1997, as amended.

On appeal docketed as CTA EB Case No. 781, the Court *En Banc* sustained the Court in Division in its Decision promulgated on February 6, 2012.

The CIR challenged *En Banc* Decision of February 6, 2012 before the Supreme Court docketed as G.R. No. 201905. It was however dismissed as the Supreme Court found no ground to warrant the reversal of the CTA *En Banc* Decision.

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[4] *En Banc* docket (CTA EB No. 1841), pp. 11-27.

Subsequently, the CIR issued a Preliminary Assessment Notice[5] (PAN) dated October 14, 2013, assessing PSH of deficiency IT, Value-added Tax (VAT), Expanded Withholding Tax (EWT) and Withholding Tax (WT) on Compensation for the TY 2009. This was followed by a Formal Assessment Notice (FAN) and Formal Letter of Demand (FLD) both dated May 23, 2014, all finding PSH liable to pay deficiency IT in the amount of Php13,180,554.95.[6]

PSH protested the FAN but it was denied in the Final Decision on Disputed Assessment[7] (FDDA) dated September 18, 2014.

PSH questioned the said FDDA before the Court in Division *via* a *Petition for Review*[8] filed on October 22, 2014 on the contention that it is entitled to the favorable declaration in the final judgments in CTA Case No. 7304, CTA EB Case No. 781, and G.R. 201905 declaring it as an institution exempt from IT. PSH argued that since the decisions in said three cases have become final and executory, they are the controlling jurisprudence as between PSH and the CIR.

In his *Answer*[9] filed on January 14, 2015, CIR countered that *res judicata* was not applicable to the present case. While there might be identity of the parties between the previous case and the case at hand, the subject matter and the cause of action were not the same. The previous case involved assessment for TY 2001, while the assessment in this case was for TY 2009. In addition, the CIR invoked the tenet that tax exemptions are construed *strictissimi juris,* hence, the essential requisites for exemption must continuously be present in order to be exempt from taxation.

Trial then ensued, during which both parties presented evidence in support of their respective positions.

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[5] Exhibit R-7.
[6] Exhibits R-9 and R-10.
[7] Exhibit R-12.
[8] Division docket, pp. 1-13.
[9] Division docket, pp. 114-125.

On July 25, 2017, the Court in Division rendered the assailed Decision[10] granting, *albeit* partially, PSH's Petition for Review.

Both aggrieved, PSH and CIR moved for a reconsideration of the Decision of July 25, 2017 but both were denied in the equally assailed Resolution[11] of March 13, 2018.

Hence, the two (2) *Petitions for Review* separately filed by the CIR and PSH docketed as CTA EB No. 1819 and CTA EB No. 1841, respectively.

In the Court *En Banc Minute Resolution* dated May 18, 2018, the two *Petitions for Review* were consolidated pursuant to Section 1, Rule 31 of the Revised Rules of Court.

On July 24, 2018, the Court *En Banc* gave due course to the consolidated *Petitions for Review* and ordered the parties to submit their respective consolidated memoranda, within thirty (30) days from notice.[12]

On October 24, 2018, the instant consolidated *Petitions for Review* were deemed submitted for decision.[13]

THE ISSUES

CIR anchors his *Petition for Review* solely on the ground that:

> THE HONORABLE COURT SECOND DIVISION ERRED IN RULING THAT RESPONDENT (PSH) IS NOT LIABLE FOR INTEREST AND COMPROMISE PENALTY IN THE AMOUNT OF Php7,329,848.06 AND Php25,000.00, RESPECTIVELY FOR TAXABLE YEAR 2009.

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[10] See Note 1, *supra*.
[11] See Note 2, *supra*.
[12] *En Banc* docket (CTA EB No. 1819), pp. 98-99.
[13] *En Banc* docket (CTA EB No. 1819), pp. 142-143.

PSH, on the other hand, submits the following issues for the resolution of the Court *En Banc,* thus:

1. Is the CIR's findings in the FDDA on the "bigness" of PSH's donation and contribution to the Congregation, Sisters of St. Paul of Charters, a "game-changing" event that justifies the application of Section 27(B) thus overriding the findings and conclusions in CTA Case No. 7304 and CTA EB No. 781 on PSH's exemption from income tax under Section 30(E)?

2. Whether or not the finding in the assailed Decision and Resolution that PSH is liable for deficiency income tax in the amount of Php8,179,619.66 is supported by evidence?

3. Whether or not the Honorable Second Division gravely erred in its analysis that the Decision of the Honorable Court *En Banc* in CTA EB No. 781 cannot be binding precedent in determining PSH's income tax exemption for taxable year 2009 because it was affirmed by the Supreme Court in a minute resolution?

In his Petition for Review, CIR submits that the Court in Division erred in holding that PSH is not liable for interest and compromise penalties having relied in good faith on the previous findings of the Court in CTA Case No. 7304. For the CIR, PSH cannot simply invoke good faith in order to escape liability from deficiency interest as Section 247(a) in relation to Section 249(B) and (C) of the NIRC of 1997, as amended, authorizes the imposition of deficiency and delinquency interest on all taxes under the NIRC.

For CIR, PSH is liable for compromise penalties in the amount of Php25,000.00 which is valid pursuant to Revenue Memorandum Order (RMO) No. 19-2007. Further, compromise penalty is not only for settlement of criminal liability but also for certain violations of the NIRC such as but not limited to failure to pay the correct internal revenue taxes. RMO No. 19-2007 has not been revoked nor declared void.

In its Comment[14], PSH contends that it protested the assessment for TY 2009 on the firm belief in good faith that the Decisions in CTA Case No. 7304 and CTA EB Case No. 781, having obtained finality, are deemed jurisprudence that the CIR must follow. Allegedly, clear is the ruling in CTA Case No. 7304 and CTA EB Case No. 781 that it is exempt from IT under Section 30(E)[15] of the NIRC.

PSH submits that there is no ambiguity in the conclusions in CTA Case No. 7304 and CTA EB Case No. 781 to the effect that PSH is exempt from IT under Section 30(E) based on <u>the possessed distinct qualification</u>. Thus, the conclusions reached in CTA Case No. 7304 and CTA EB Case No. 781, unless overturned, demand adherence.

PSH also contends that the findings in the assailed Decision and Resolution prove the merit of its plea for the reversal of the assessed deficiency IT under Section 27(B)[16] amounting to Php8,179,619.66. PSH further posits that the assailed Decision indicates that it was able to prove by substantial evidence that its contribution inured to the benefit of, or supported the activities of SPC reinforcing its character and qualification as a non-stock, non-profit,

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[14] *En Banc* docket (CTA EB No. 1819), pp. 78-96.

[15] Sec. 30. Exemption from Tax on Corporations. — The following organizations shall not be taxed under this Title in respect to income received by them as such:

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.

[16] 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 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.

religious and charitable institution exempt from income tax under Section 30(E) of the NIRC.

PSH also disagrees with the conclusion of the Court in Division that the ruling in CTA EB Case No. 781 could not qualify under the doctrine on conclusiveness of judgment and could not be considered as a binding precedent as it was affirmed by the Supreme Court only through a minute resolution. PSH asserts that a minute resolution dismissing a Petition for Review filed under Rule 45 of the Rules of Court constitutes an actual adjudication on the merits as pronounced by the Supreme Court in *Agoy vs. Araneta Center, Inc.*[17]

PSH stresses that as established, it is, and remains to be a non-stock, non-profit, religious and charitable institution, and no part of its income inure directly or indirectly to the benefit of any specific person. Thus, following the Supreme Court's ruling in *Sea-Land Service Inc. vs. CA*,[18] the conclusions in CTA Case No. 7304 and CTA EB No. 781 is the law of the case, and bar its re-litigation under the doctrine on conclusiveness of judgment.

In its *Comment*[19], CIR sides with the Court in Division saying that it correctly ruled that PSH is liable for deficiency IT for TY 2009.

The CIR reiterated his positions stated in his Answer dated January 14, 2015 filed with the Court in Division saying that while there could possibly be identity of the parties between the previous cases and the case at bar, the subject matter and the cause of action however are not the same. The subject matter in CTA Case No. 7304 was the assessment for TY 2001 while, the present case is for assessment for TY 2009. He again points out that tax exemptions are construed *strictissimi juris*. The requirements provided by law for tax exemption must be continually satisfied by the taxpayer in order to enjoy immunity from taxation. As such, he is not precluded from conducting an investigation in order to ensure that the

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[17] G.R No. 196358, March 21, 2012.
[18] G.R. No. 122605, April 30, 2001.
[19] *En Banc* docket (CTA EB No. 1819), pp. 73-76.

taxpayer continuously meets the criteria for exemption for each TY.

The Court *En Banc's* Ruling

Both *Petitions for Review* lack merit.

CTA EB No. 1819 (CIR's Petition for Review):

Irrefragably, the arguments raised by the CIR in his Petition for Review were truncated from his pleading filed with the Court in Division, specifically from his Answer dated January 14, 2015. There is no new issue raised which has not been discussed and passed upon by the Court in Division in the assailed Decision dated July 25, 2017, as well as, in the assailed Resolution dated March 13, 2018. The Court *En Banc* sees no compelling reason to deviate from the findings of the Court in Division that the assessment for interest and compromise penalty should be deleted on the basis of good faith and honest belief on the part of PSH that it is not subject to IT.

As the Supreme Court declared in several cases[20], good faith and honest belief that one is not subject to tax on the basis of previous interpretations of government agencies tasked to implement the tax law are sufficient justification to delete the imposition of surcharges and interest.

In *Michel J. Lhuillier Pawnshop, Inc. vs. CIR,*[21] the Supreme Court held, thus:

> Nevertheless, all is not lost for petitioner. The settled rule is 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**

[20] *Michel J. Lhuillier Pawnshop, Inc. vs. Commissioner of Internal Revenue*, G.R. No. 166786, September 11, 2006; *Antam Pawnshop Corporation vs. Commissioner of Internal Revenue*, G.R. No.167962, September 19, 2008; and *Tambunting Pawnshop, Inc. vs. Commissioner of Internal Revenue*, G. R. No. 179085, January 21, 2010.
[21] G.R. No. 166786, September 11, 2006.

> **imposition of surcharges and interest.** In *Connell Bros. Co. (Phil.) v. Collector of Internal Revenue*, it was held that:
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> > We are convinced that appellant, in preparing its sales invoices as it did, was not guilty of an intentional violation of the law. It did not delay filing the returns for the sales taxes corresponding to the period in question, let alone did so purposely. The delay was in the payment of the deficiency, which arose from a mistaken understanding of the regulations laid down by appellee. The ensuing controversy was, in our opinion, generated in good faith and should furnish no justification for the imposition of a penalty.
> >
> > xxx xxx xxx
>
> This ruling was subsequently reiterated in *Tuason, Jr. v. Lingad*, where we deleted the order to pay interest and surcharges, and in *Commissioner of Internal Revenue v. Republic Cement Corporation*, where the same surcharge was dispensed with because of the taxpayer's good faith and the BIR's previous erroneous interpretation of the laws involved. We see no reason not to apply the same doctrine in the instant case which settles the divergent rulings of the BIR on DST and establishes the foremost categorical pronouncement of the Court that pledge transactions entered into by pawnshops are subject to DST. (*Emphasis supplied; Citations omitted*)

In the recently decided case of *Commissioner of Internal Revenue vs. St. Luke's Medical Center, Inc.,*[22] the Supreme Court reaffirmed the foregoing doctrine, as follows:

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[22] G.R. No. 203514, February 13, 2017.

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> 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. (*Underscoring and boldfacing supplied*)

In the instant case, the record is pregnant with indications that PSH honestly believed in good faith that it is not liable to pay the tax assessed by virtue of the previous pronouncement of the Court in CTA Case No. 7304, which the Supreme Court effectively affirmed in G.R. No. 201905. Hence, the Court *En Banc* finds no reason not to apply the foregoing ruling deleting the assessment for interest and compromise penalty for TY 2009.

CTA EB No. 1841 (PSH's Petition for Review):

PSH's Petition for Review deserves scant consideration. After a judicious review of PSH's arguments and the record of the case, the Court *En Banc* as well finds no reason to modify much more reverse the assailed Decision and Resolution of the Court in Division.

A revisit of the arguments raised by PSH shows that they have been amply discussed and passed upon by the Court in Division in the assailed Decision of July 25, 2017 and Resolution dated March 13, 2018. But if only to give emphasis to salient points of the assailed Decision, the Court *En Banc* will discuss them anew.

In relation to the issue of whether the Court in Division erred in its analysis that the Decision of this Court's En Banc in CTA EB Case No. 781 cannot qualify under the doctrine on conclusiveness of judgment and cannot be considered as a binding precedent as it was affirmed by the Supreme Court only through a minute resolution, the ruling of the Supreme Court in the case of *Social Security Commission vs. Rizal Poultry and Livestock Association, Inc., et al.*,[23] is glaringly on the point, to wit:

> 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 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**.

As the Court in Division correctly laid down, **the evidence presented in CTA Case No. 7304[24] was <u>not</u> directly controverted**. Thus, the judgment thereon cannot be considered as a conclusively settled fact or question.

It is also well to note that aside from the fact that the **instant case involves PSH's income for TY 2009**, the appealed FDDA also indicates that PSH declared in its 2009 audited financial statement that it gave donations and support totaling to Php10,968,632.59 (lodged as part of general and administrative expenses) to the Sisters of St. Paul of Chartres, the congregation that formed and operates

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[23] G.R. No. 167050, June 1, 2011.
[24] *Perpetual Succour Hospital of Cebu, Inc., and the Sisters of St. Paul the Chartres vs. Commissioner of Internal Revenue*, CTA Case No. 7304, December 1, 2010.

PSH. To be sure, these matters were not considered in the Decision of the Court in Division in CTA Case No. 7304, which was affirmed in CTA EB Case No. 781 and, the Supreme Court in G.R. No. 201905, as the same only involves transactions made for TY 2001.

Thus, the Court *En Banc* agrees with the Court in Division on this point - that the doctrine of conclusiveness of judgment does not apply in this case.

Likewise, the Court En Banc agrees with the Court in Division in holding that the minute resolution issued by the Supreme Court in G.R. No. 201905, which effectively affirmed the ruling in CTA EB Case No. 781, is not a binding precedent.

In the case of *Deutsche Bank AG Manila Branch vs. Commissioner of Internal Revenue,*[25] citing the case of *Philippine Health Care Providers, Inc. vs. Commissioner of Internal Revenue,*[26] the Supreme Court clarified the concept of a minute resolution, as follows:

> 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:
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> > 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

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[25] G.R. No. 188550, August 19, 2013.
[26] G.R. No. 167330, September 18, 2009.

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 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.
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> 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. (*Emphasis supplied; citations omitted*)

As the Court in Division clearly pointed out, the fact alone that the Court ruled in the previous case that petitioner is exempt from payment of IT for TY 2001, which was affirmed by the Supreme Court in a minute resolution, is **not a binding precedent in determining PSH's IT exemption for TY 2009**.

On its alleged exemption from the payment of the 10% preferential income tax rate under Section 27(B) of the NIRC of 1997, as amended, PSH asserts that the assailed Decision indicates that it was able to establish that the contribution it gave inured to the benefit of, or supported the activities of SPC reinforcing its found character and qualification as a non-stock, non-profit, religious and charitable institution exempt from income tax under Section 30(E) of the NIRC.

The Court *En Banc* is not convinced.

Note that under Section 30(E) of the NIRC of 1997, as amended, **<u>one</u>** of the requirements for a charitable institution to be exempt from income tax is 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, thus:

> Sec. 30. *Exemption from Tax on Corporations.* — The following organizations shall not be taxed under this Title in respect to income received by them as such:
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> 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**. (*Emphasis supplied*)

The Supreme Court, in the case of *Commissioner of Internal Revenue vs. St. Luke's Medical Center, Inc.*,[27] extensively elucidated the application of Section 27(B), in relation to Section 30(E) of the NIRC of 1997, as amended, as follows:

> 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)**

[27] G.R. Nos. 195909 and 195960, September 26, 2012.

instead of the ordinary 30% corporate rate under the last paragraph of Section 30 in relation to Section 27(A)(I).

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 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 nonprofit 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 outpatient, 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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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.

In fine, for the exemption under Section 30(E) of the NIRC of 1997, as amended, to apply, the charitable institution must likewise be operated **exclusively** for charitable purposes.

On this point, it is worth to note the observation of the Court in Division that PSH failed to present evidence to overcome CIR's finding that the hospital is an institution NOT "**operated exclusively**" for charitable purpose. In the assailed FDDA, CIR found that for TY 2009, PSH had revenues of Php675,892,543.00 from services rendered to paying patients. For the CIR, revenues from paying patients are income received from activities conducted for profit.

The Surpreme Court in the same *St. Luke's* case[28], further ruled, 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 x x x charitable x x x purposes x x x.' 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**

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[28] See Note 28, *supra*.

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%.

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.'** Indeed, St. Luke's admits that it derived profits from its paying patients. St. Luke's declared P1,730,367,965 as 'Revenues from Services to Patients' in contrast to its 'Free Services' expenditure of P218,187,498. 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 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.'**

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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).**
>
> 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. (*Emphasis supplied*)

Clearly, 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.'

Thus, as correctly pointed out by the Court in Division, even if petitioner is considered to have satisfied the requirement 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," the imposition of the 10% preferential tax rate under Section 27(B) of the NIRC of 1997, as amended, must be sustained since PSH failed to controvert CIR's finding that PSH is not "operated exclusively for charitable purpose" for the TY 2009.

WHEREFORE, the *Petitions for Review* filed on April 13, 2018 and May 10, 2018 by the Commissioner of Internal Revenue and Perpetual Succour Hospital of Cebu, Inc., respectively, are hereby **DENIED** for lack of merit. Accordingly, the assailed Decision and Resolution dated July 25, 2017 and May 13, 2018, respectively, are **AFFIRMED**.

SO ORDERED.

ESPERANZA R. FABON-VICTORINO
Associate Justice

We Concur:

ROMAN G. DEL ROSARIO
Presiding Justice

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

ERLINDA P. UY
Associate Justice

CIELITO N. MINDARO-GRULLA
Associate Justice

MA. BELEN RINGPIS-LIBAN
Associate Justice

CATHERINE T. MANAHAN
Associate Justice

JEAN MARIE A. BACORRO-VILLENA
Associate Justice

MARIA ROWENA MODESTO-SAN PEDRO
Associate Justice

CERTIFICATION

Pursuant to Section 13, Article VIII of the Constitution, it is hereby certified that the conclusions in the above Decision were reached in consultation before the cases were assigned to the writer of the opinion of the Court.

ROMAN G. DEL ROSARIO
Presiding Justice