

REPUBLIC OF THE PHILIPPINES
Court of Tax Appeals
QUEZON CITY

SECOND DIVISION

ST. LUKE'S MEDICAL CENTER,
INC.,

Petitioner,

-versus-

COMMISSIONER OF INTERNAL
REVENUE,

Respondent.

CTA CASE NO. **7789**

Members:

CASTAÑEDA, JR. *Chairperson*
CASANOVA, and
MINDARO-GRULLA, J.J.

Promulgated:

AUG 26 2010

X-----X
✓ 3:55 p.m.

DECISION

MINDARO-GRULLA, J.:

This is a Petition for Review filed by petitioner St. Luke's Medical Center, Inc. seeking the cancellation and withdrawal of the assessments issued against petitioner for alleged deficiency income taxes for the taxable years 2005 and 2006, in the total amount of P142,679,408.15, on the ground that petitioner is exempt from tax, pursuant to Sections 30(E) and (G) of the National Internal Revenue Code (NIRC) of 1997, as amended. 6

Petitioner St. Luke's Medical Center, Inc. is a non-stock, non-profit corporation duly organized and existing under the laws of the Philippines, with principal place of business located at 279 E. Rodriguez Sr. Blvd., Cathedral Heights, Quezon City.¹

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. He holds office at the BIR National Office Building, BIR Road, Diliman, Quezon City.

On December 14, 2007, petitioner received from the Large Taxpayers Service-Document Processing and Quality Assurance Division, the following:

Audit Results/Assessment Notice No. (with Assessment Notice Attachment)	For	Taxable Year	Amount
QA-07-000096	Deficiency income tax	2005	P78,617,434.54
QA-07-000097	Deficiency income tax	2006	P57,119,867.33
TOTAL			P135,737,301.87

thus, Audit Results/Assessment Notice Nos. QA-07-000096 and QA-07-000097, both dated November 22, 2007, assessed petitioner deficiency income tax in the amount of P78,617,434.54 for the taxable year 2005 and P57,119,867.33 for the taxable year 2006.²

¹ Exhibit "E"

² Exhibits "A", "A-1", "A-2", "B", "B-1", and "B-2"; par. 3, Stipulation of Facts, Joint Stipulation of Facts and Simplification of Issues, docket, p. 207

Petitioner, disagreeing with the foregoing assessments, filed an administrative protest on January 14, 2008.³

On April 25, 2008, petitioner received the Final Decision on Disputed Assessment, which modified the Audit Results/Assessment Notices by increasing the amount of alleged deficiency income tax for the year 2005 to P82,419,522.21 and for the year 2006 to P60,259,885.94, or a total amount of P142,679,408.15.⁴

The alleged deficiency income taxes for the taxable years 2005 and 2006 were computed by respondent in the following manner:⁵

ASSESSMENT NO. QA-07-000096

PARTICULARS	AMOUNT
Sales/Revenues/Receipts/Fees	P 3,623,511,616.00
Less: Cost of Sales/Services	2,643,049,769.00
Gross Income From Operation	980,461,847.00
Add: Non-Operating & Other Income	-
Total Gross Income	980,461,847.00
Less: Deductions	481,266,883.00
Net Income Subject to Tax	499,194,964.00
x Tax Rate	10%
Tax Due	49,919,496.40
Less: Tax Credits	-
Deficiency Income Tax	49,919,496.40
Add: Increments	
25% Surcharge	12,479,874.10
20% Interest Per Annum (4/15/06-4/15/08)	19,995,151.71
Compromise Penalty for Late Payment	25,000.00
Total Increments	32,500,025.81
Total Amount Due	P 82,419,522.21

³ Exhibits "C" and "C-1"

⁴ Exhibits "D" and "D-1"

⁵ Exhibit "D"

ASSESSMENT NO. QA-07-000097

PARTICULARS	AMOUNT
Sales/Revenues/Receipts/Fees	P3,815,922,240.00
Less: Cost of Sales/Services	2,760,581,437.00
Gross Income From Operation	1,055,403,803.00
Add: Non-Operating & Other Income	-
Total Gross Income	1,055,403,803.00
Less Deductions	640,147,719.00
Net Income Subject to Tax	415,256,084.00
x Tax Rate	10%
Tax Due	41,525,608.40
Less: Tax Credits	-
Deficiency Income Tax	41,525,608.40
Add: Increments	
25% Surcharge	10,381,402.10
20% Interest Per Annum (4/15/07-4/15/08)	8,327,875.44
Compromise Penalty for Late Payment	25,000.00
Total Increments	18,734,277.54
Total Amount Due	P 60,259,885.94

The tax assessment on petitioner's income was based on allegations that petitioner falls within Section 27(B) of the NIRC of 1997, as amended.

In the Final Decision on Disputed Assessment, respondent stated the following findings:

"The assessments arose from your non-payment of income tax due per return for the taxable years 2005 and 2006. This is based on Section 27(B) of the National Internal Revenue Code, as amended, which provides, among others, that proprietary educational institutions and hospitals, which are non-profit, shall pay a tax of ten percent (10%) on their taxable income.

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The BIR and the subject assessments do not in any way question the nature of SLMC's organization and corporate structure, rather the assessment notices and collection letters were issued based on the clear provisions of Section 27(B) of the Tax Code that non-profit hospitals are now liable to pay ten percent (10%) on its taxable income." *l*

Respondent also imposed a twenty-five percent (25%) surcharge on petitioner based on Section 248(A)(1) of the NIRC of 1997, as amended, which provides⁶:

"SEC. 248. *Civil Penalties.* –

(A) There shall be imposed, in addition to the tax required to be paid, a penalty equivalent to twenty-five percent (25%) of the amount due, in the following cases:

- (1) Failure to file any return and pay the tax due thereon as required under the provisions of this Code or rules and regulations on the date prescribed; or"

After receipt of respondent's final decision on its protest, petitioner filed the instant Petition for Review on May 23, 2008.

In his Answer⁷, respondent raised the following Special and Affirmative Defenses:

- "4. Petitioner is subject to 10% income tax. Section 27 (B) of the NIRC of 1997 specifically provides that:

x x x x x x

5. Crystal clear from the foregoing provision of law is the fact that non-profit hospitals are now liable to pay ten percent (10%) on their taxable income except those covered by Section (D) of the same Code. This is a new provision introduced by the legislature unmistakably intended to amend the exemption on non-profit hospitals that were previously categorized as non-stock, non-profit corporations under Section 26 of the NIRC of 1977, as amended.
6. The aforequoted provision should be distinguished from Section 30(E) of the NIRC of 1997 which provides:

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⁶ Par. 15, Stipulation of Facts, Joint Stipulation of Facts and Simplification of Issues, Docket, p. 213

⁷ Docket, pp. 147-152

7. 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.
8. Moreover, 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 hospitals 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%.
9. Petitioner's reliance on the alleged letter of exemption issued to it on 9 June 1990 stating among others that it falls within the purview of a corporation for purely charitable and social welfare purposes, and accordingly, it is exempt from the payment of income tax on income received by it as such organization is utterly misplaced. In light of the enactment of the NIRC of 1997 which took effect on 1 January 1998, the 1990 ruling being invoked by petitioner is deemed repealed by Section 27(B). Thus, petitioner, as non-profit hospital is now subject to the 10% tax on its taxable income.

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10. The payment of surcharge is mandatory. It has been explained by the Supreme Court 'xxx 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. xxx' (*Philippine Refining Company vs. Court of Appeals, et al.*, G.R. No. 118794, 8 May 1996).
11. Compromise penalties were imposed for failure of petitioner to file the quarterly income tax returns. *ℓ*

12. The claims of the Petitioner that no specific person including the trustees, officers and employees do not directly benefit from its profits and assets, lacks any basis.
13. Well-settled is the rule that tax assessments are entitled to the presumption of correctness and made in good faith. The taxpayer has the duty to prove otherwise. In the absence of proof of any irregularities in the performance of duties, an assessment duly made by a Bureau of Internal Revenue examiner and approved by his superior officers will not be disturbed. All presumptions are in favor of the correctness of tax assessments. (*Sy Po vs. Court of Tax Appeals*, 164 SCRA 524)."

During trial, petitioner presented documentary and testimonial evidence to support its claims and contentions; while respondent, through counsel, manifested that he will not present any witness.⁸

On January 22, 2010, the Court issued a Resolution⁹ submitting the case for decision, considering petitioner's Memorandum filed on January 8, 2010¹⁰ and respondent's Memorandum filed on January 7, 2010.¹¹

The parties raised the issues¹² as follows:

- "1. Whether Petitioner is exempt from or subject to 10% Income Tax.
2. Whether Petitioner failed to exhaust all administrative remedies before filing the instant petition with this Honorable Court thereby making the instant petition dismissible.
3. Whether Petitioner is liable for compromise penalties for alleged non-compliance with Section 248 (A) of the NIRC, as amended."

⁸ Docket, p. 952

⁹ Docket, p. 1058

¹⁰ Docket, pp. 960-1002

¹¹ Docket, pp. 953-958

¹² Docket, p. 213

But the main issue in the instant case is whether petitioner is exempt from income tax under Section 30(E) and (G) of the NIRC of 1997, as amended, or liable to pay ten percent (10%) income tax, in accordance with Section 27(B) of the same Code.

Respondent found petitioner liable for deficiency income tax for the taxable years 2005 and 2006 based on Section 27(B) of the NIRC of 1997, as amended, which reads as follows:

"SEC. 27. *Rates of Income Tax on Domestic Corporations.* -

(B) *Proprietary Educational Institutions and Hospitals.* - Proprietary educational institutions and hospitals which are nonprofit shall pay a tax of ten (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."

Petitioner claims that it is exempt from payment of income tax, citing Section 30(E) and (G) of the NIRC of 1997, which states as follows: 6

"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) Non-stock 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;

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(G) Civic league or organization not organized for profit but operated exclusively for the promotion of social welfare."

In the case of *St. Luke's Medical Center, Inc. vs. Commissioner of Internal Revenue*¹³, this Court already settled the issue as to the tax treatment of petitioner's income, petitioner being a non-stock, non-profit hospital. In the said case, this Court had the occasion to distinguish between Section 27(B) and Section 30(E) and (G).

We quote the pertinent portions of the said Decision for ready reference, to wit:

"The difference between Sections 27 (B) and 30 (E) of the NIRC of 1997, as amended, is clear. To fall under Section 27 (B), the hospital must be a non-profit corporation or association. However, unlike Section 30 (E), Section 27 (B) does not require that the hospital must be a non-stock corporation.

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Since Section 27 (B) of the NIRC of 1997, as amended, expressly provides that 'proprietary educational institutions and hospitals which are non-profit shall pay a tax of ten

¹³ CTA Case No. 6993, November 21, 2008 6

percent (10%) on their taxable income', it necessarily follows that when a hospital is non-stock, non-profit, and operated exclusively for charitable purpose, it falls within the purview of *Section 30 (E) of the NIRC of 1997, as amended*, and not under *Section 27 (B) of the same Code*.

This intention of the legislature to exempt 'non-stock, non-profit corporations/associations operated exclusively for charitable purpose' is evident, when the legislature incorporated the word 'Non-stock' before the phrase 'corporation or association organized and operated exclusively for religious, charitable, scientific, athletic, or cultural purposes ...' of the former *Section 26 of the NIRC of 1977, as amended. xxx*"

Based on the foregoing, it is evident that when a hospital is a non-stock and non-profit corporation/association operated exclusively for charitable purpose, the income received by it as such is exempt from income tax under *Section 30(E) of the NIRC of 1997, as amended*.

In other words, for *Section 30(E) and (G) of the NIRC of 1997* to apply in the instant case, petitioner must establish –

- (1) that it is a non-stock corporation;
- (2) that it is operated exclusively for charitable purpose; and
- (3) 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.

Anent the first requirement, petitioner is registered with the Securities and Exchange Commission as a non-stock, non-profit corporation, as indicated in its Amended Articles of Incorporation¹⁴. It

¹⁴ Exhibits "E" and "E-1" 6

is composed of trustees instead of stockholders, and no part of its income is distributed as dividends to its trustees.¹⁵

As regards the second requisite, the stated objectives and purposes in the same Amended Articles of Incorporation are charitable in character. It mentions of the incorporators' primary purpose in forming a charitable and social welfare institution. Petitioner's objectives and purposes, as indicated in its Amended Articles of Incorporation, are as follows:

"(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;

(b) To provide a center of health sciences education and provide medical services to the community through organized clinics in such specialties as the facilities and resources of the corporation may make possible;

(c) To carry on educational activities related to the maintenance and promotion of health as well as provide facilities and for scientific and medical researches which, in the opinion of the Board of Trustees, may be justified by the facilities, personnel, funds or other requirements that are available;

(d) To cooperate with organized medical societies, agencies of both government and private sector; establish rules and regulations consistent with the highest professional ethics;

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Moreover, its existence as a charitable and social welfare institution is recognized by different government and non-government

¹⁵ Exhibits "SSSS" and "UUUU" 6

organizations, such as the National Council of Social Development Foundation of the Philippines, Inc., the Department of Social Welfare and Development, and the Philippine Charity Sweepstakes Office (PCSO), among others, as mentioned in the Judicial Affidavit¹⁶ of Ms. Cristina S. Hangod. Ms. Hangod is the Manager and Head of petitioner's Medical Social Service Department.

In support of the contention that it operates exclusively for charitable purpose, petitioner submitted the exhibits showing its charitable and social welfare activities, as follows:

EXHIBIT	DESCRIPTION
"L"	Municipality of Sipalay, Negros Occidental, Municipal Council Resolution No. 99-210, "A Resolution thanking the St. Lukes Medical Center, thru its President and Chief Executive Officer Jose F.G. Ledesma and Outreach Program Coordinator Ellen S. Gawigawen relative to the donation of various medical equipment for the lying-in clinic of the Municipality of Sipalay, Negros Occidental", adopted on November 3, 1999
"L-1"	Letter of Sipalay Municipal Mayor Oscar C. Montilla, Jr. addressed to Mr. Jose F.G. Ledesma, President/CEO of St. Luke's Medical Center dated November 15, 1999
"M"	Province of Capiz, Roxas City Resolution No. 306, Series of 1999, "Authorizing the Honorable Vicente B. Bermejo to enter into a Memorandum of Agreement for a Hospital Twinning Program with St. Luke's Medical Center (SMLC) for and in behalf of the Province of Capiz", adopted on December 3, 1999
"N"	Memorandum of Agreement between Roxas Memorial Provincial Hospital and St. Luke's Medical Center dated December 7, 1999
"O"	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",

¹⁶ Exhibit "QQQ" 2

	adopted March 18, 2002
"P"	Letter of Municipal Mayor Jerry M. Tabujara of the Municipality of Cauayan, Negros Occidental addressed to Ms. Ellen Gawin-Gawin of St. Luke's Medical Center dated March 31, 2000
"Q"	Letter from the Office of the Provincial Governor, Province of Nueva Vizcaya, expressing gratitude for the medical-dental mission of the Sagip Bayan Foundation and SLMC dated October 23, 2004
"R"	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
"T"	Letter from St. Theodore's Hospital addressed to St. Luke's Medical Center, acknowledging receipt of funds for hospital renovations, dated February 1, 2002
"U"	Letter of gratitude dated June 7, 2002 from St. Theodore's Hospital for the donation of St. Luke's Medical Center of an Anesthesia Machine
"V"	Letter from Fr. Mer and Deisy Karganilla of the Juan S. Alano Memorial Hospital, Inc., Isabela, Basilan Province addressed to Ms. Ellen Gawigawen of St. Luke's Medical Center dated March 21, 2001
"W"	Letter of Appreciation from the Air Force General Hospital dated February 6, 2004 addressed to Ms. Ellen Gawigawen
"X"	Letter from Sister Teresita Montanano of White Cross Children's Home addressed to the Manager of St. Luke's Medical Center dated September 25, 2002
"Y"	Letter of appreciation dated January 15, 2002 from Nelia F. Treseñe of Bahay Pangarap addressed to Mr. Jose Ledesma, President of St. Luke's Medical Center
"Z"	Certificate of Appreciation from Lunday Study Center for the free medical services rendered to the residents of Parel, Bangan and Botolan, Zambales dated June 10, 2004
"AA"	Letter from The Episcopal Diocese of Northern Philippines addressed to Mr. Jose Ledesma, President and Chief Executive Officer of St. Luke's Medical Center acknowledging receipt of donation dated November 23, 2001
"BB"	Letter from the Episcopal Diocese of Southern Philippines dated June 9, 2004, acknowledging receipt of P700,000 for

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	the construction of church building in Isulan Sultan Kudarat
"CC" and "CC-1"	Episcopal Diocese of Southern Philippines Official Receipt No. 16122 dated October 22, 2004, issued to SLMC for the amount of P400,000.00 (for the construction of Church building in Isulan, Sultan Kudarat)
"DD"	Episcopal Diocese of Southern Philippines Certification of Receipt issued to SLMC for the amount of P619,000.00 (for the construction of Church building in Isulan, Sultan Kudarat)
"EE"	Episcopal Diocese of Southern Philippines Certification of Receipt issued to SLMC for the amount of P800,000.00 (for the construction of Church building in Isulan, Sultan Kudarat)
"HH"	Contract of Agreement between National Children's Hospital and St. Luke's Medical Center dated November 18, 1999
"II"	Memorandum of Agreement between PCSO and St. Luke's Medical Center dated July 6, 2001
"JJ"	Memorandum of Agreement between PCSO and St. Luke's Medical Center dated September 24, 1998
"QQ-1"	Cash Voucher No. 3600040534 dated December 28, 2005, under the name of Episcopal Diocese of Northern Phils., Inc. amounting to P304,000.00 (initial assistance for tire pathing of trail to Holy Innocent)
"SS"	Episcopal Diocese of Northern Philippines Official Receipt No. 11212 dated July 26, 2007, amounting to P200,000.00
"SS-1"	Cash Voucher No. 3600008937 dated July 4, 2007, under the name of Episcopal Diocese of Northern Phils., Inc., amounting to P200,000.00 (second release assistance for tire pathing work of trail to Holy Innocent)
"UU-1"	Cash Voucher No. 3600010412 dated June 14, 2005 under the name of Episcopal Diocese of Northern Phils., Inc. amounting to P863,475.00 (for the completion of St. Philip Church)
"AAA"	The St. Theodore of Tarsus Hospital Foundation Official Receipt No. 0915 dated March 27, 2006, amounting to P1,000,000.00
"QQQ"	Judicial Affidavit of Christina Hangod, executed on August 13, 2008
"RRRR"	Judicial Affidavit of Ellen Gawigawen, executed on October 27, 2008
"SSSS"	Judicial Affidavit of Rt. Rev. Manuel Lumpias, executed on

	November 25, 2008
"TTTT"	Petitioner's Statement of Revenues and Expenses and Schedule of Free Service Allocation for the taxable years 2005 and 2006 prepared by petitioner's Accounting Manager, Mr. Romeo B. Mary
"UUUU"	Judicial Affidavit of Romeo B. Mary, executed on February 5, 2009

Significantly, the issue of whether petitioner is a charitable institution had been resolved by the Supreme Court in the case of *Commissioner of Internal Revenue vs. Bishop of the Missionary District of the Philippine Islands of the Protestant Episcopal Church in the U.S.A. and the Court of Tax Appeals*¹⁷, in this wise:

"Again, it should be enough to point out that the admission of pay patients does not detract from the charitable character of a hospital, if, as in the case of St. Luke's Hospital, its funds are devoted exclusively to the Maintenance of the institution (Cf., e.g., *Herrera v. Quezon City Board of Assessment Appeals*, G.R. No. 15270, September 30, 1961). The Secretary of Finance cannot limit or otherwise qualify the enjoyment of this exemption granted under Republic Act No. 1916 in implementing the law."

In the more recent case of *St. Luke's Medical Center, Inc. vs. Commissioner of Internal Revenue*¹⁸, promulgated on February 23, 2009, this Court's First Division confirmed petitioner's charitable character, expounding that petitioner does not lose its charitable character despite earning income from its patrons, citing the case of *Hospital De San Juan De Dios, Inc. vs. Pasay City, Pablo Cuneta, R. N.*

¹⁷ G.R. No. L-19445, August 31, 1995

¹⁸ CTA Case No. 6746, February 23, 2009

Ascaño and G. C. Fuentes¹⁹, the pertinent portions of which we quote, as follows:

"Moreover, the question of whether or not appellant and other institutions similarly situated and operated are charitable institutions has been decided both here and in the United States. The American rule is summarized in 51 American Jurisprudence, p. 607, as follows:

636. *Effect of Receipt of Pay from Patients.*

The general rule that a charitable institution does not lose its charitable character and its consequent exemption from taxation merely because recipients of its benefits who are able to pay are required to do so, where funds derived in this manner are devoted to the charitable purposes of the institution, applies to hospitals. A hospital owned and conducted by a charitable organization, devoted for the most part to the gratuitous care of charity patients, is exempt from taxation as a building used for 'purposes purely charitable', notwithstanding it receives and cares for pay patients, where any profit thus derived is applied to the purposes of the institution. An institution established, maintained, and operated for the purpose of taking care of the sick, without any profit or view to profit, but at a loss, which is made up by benevolent contributions, the benefits of which are open to the public generally, is a purely public charity within the meaning of a statute exempting the property of institutions of purely public charity from taxation; the fact that patients who are able to pay are charged for services rendered, according to their ability, being of no importance upon the question of the character of the institution.

On the other hand, in *Jesus Sacred Heart College vs. Collector, etc.*, G.R. No. L-6807, May 20, 1954, We overruled the contention of the Collector of Internal Revenue to the effect that the fact that the appellant herein had a profit or net income was sufficient to show that it was an institution 'for profit and gain' and therefore no longer exempt from income tax as follows:

¹⁹ G.R. No. L-19371, February 28, 1966

To hold that an educational institution is subject to income tax wherever it is so administered as to reasonably assure that it will not incur a deficit, is to nullify and defeat the aforementioned exemption. Indeed, the effect, in general, of the interpretation advocated by appellant would be to deny the exemption whenever there is a net income, contrary to the tenor of said Section 27 (e) which positively exempts from taxation those corporations which, otherwise, would be subject thereto, because of the existence of said net income.

Explaining our view that the making of profit does not destroy the tax exemption of a charitable, benevolent or educational institution, We said:

Needless to say, every responsible organization must be so run as to at least, insure its existence, by operating within the limits of its own resources, especially its regular income. In other words, it should always strive, whenever possible, to have a surplus. Upon the other hand, appellant's pretense, would limit the benefits of the exemption, under said Section 27 (e), to institutions which do not hope, or propose, to have such surplus. Under this view, the exemption would apply only to schools which are on the verge of bankruptcy, for — unlike the United States, where a substantial number of institutions of learning are dependent upon voluntary contributions and still enjoy economic stability, such as Harvard, the trust fund of which has been steadily increasing with the years — there are, and there have always been very few educational enterprises in the Philippines which are supported by donations, and those organizations usually have a very precarious existence. The final result of appellant's contention, if adopted, would be to discourage the establishment of colleges in the Philippines, which is precisely the opposite of the objective consistently sought by our laws.

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In line with the foregoing, in *U.S.T. Hospital Employees Association vs. Santo Tomas University Hospital* (G.R. No. L-6988, decided May 24, 1954), we held that the U.S.T. Hospital 

was not established for profit-making purposes, despite the fact that it had 140 paying beds, because the same were maintained only to 'partly finance the expenses of the free wards', containing 203 beds for charity patients. Although said case involved the interpretation of Republic Act No. 772, it is patent from our decision therein that said institution was not considered engaged in 'business'.

It is trite to say that a tax on the limited revenue of charitable institutions of this kind tends to hamper its operation, and accordingly, to discourage the establishment and maintenance thereof. In the absence of a clear legal provision thereon, we must not so construe our laws as to lead to such result. In other words, the second, third and fourth assignments of error are untenable.

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Finally, in *Manila Sanitarium and Hospital vs. Gabuco*, G.R. No. L-14331, January 31, 1963, We held that the mere charging of medical and hospital fees from those who could afford to pay, did not make the institution one established for profit or gain.' (*Emphasis supplied*)

As petitioner is a non-stock, non-profit corporation organized for charitable and social welfare purpose, it is exempt from paying income taxes under Section 30 (E) and (G) of the NIRC, which reads:"

The operation of the hospital is the very means it meets its purpose of performing charitable activities. It is the income from hospital operation that sustains not only the charitable works of the hospital, but more importantly, the very existence of the said institution. Petitioner's income from its operation as a hospital does not strip it of its charitable character. Hence, petitioner is considered to be operated exclusively for charitable purpose.

On the third requisite, one of the members of the Board of Trustees of petitioner, Rt. Rev. Manuel C. Lumpias, in his Judicial 6

This Court agrees with respondent that petitioner's exemption from income tax does not extend to income of whatever kind from its properties, real or personal, or from any of its activities conducted for profit.

However, records show that petitioner had no "non-operating and other income" for the taxable years 2005 and 2006. This is confirmed by the Annual Income Tax Returns of petitioner for the taxable years 2005²² and 2006²³, as well as respondent's Final Decision on Disputed Assessment²⁴, which did not reflect any "non-operating and other income" incurred for the taxable years 2005 and 2006.

Consequently, since petitioner is exempt from payment of income tax, respondent's assessment against petitioner for deficiency income tax and the included compromise penalties and surcharges should be cancelled and set aside.

As to the issue of non-exhaustion of administrative remedies, petitioner was able to file a letter of protest on January 14, 2008 against respondent's deficiency tax assessments. In fact, respondent issued a Final Decision on Disputed Assessment on April 9, 2008, taking into consideration the protest filed by petitioner. Petitioner is deemed to have exhausted the administrative remedies available to it before filing the instant Petition for Review.

²² Exhibit "H"

²³ Exhibit "I"

²⁴ Exhibit "D" *L*

WHEREFORE, premises considered, the Petition for Review is hereby **GRANTED**. Accordingly, Audit Results/Assessment Notice Nos. QA-07-000096 and QA-07-000097, assessing petitioner for alleged deficiency income taxes for the taxable years 2005 and 2006, respectively, are hereby **CANCELLED** and **SET ASIDE**.

SO ORDERED.


CIELITO N. MINDARO-GRULLA
Associate Justice

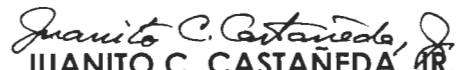
WE CONCUR:


JUANITO C. CASTAÑEDA, JR.
Associate Justice


CAESAR A. CASANOVA
Associate Justice

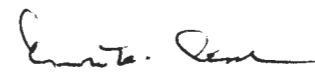
ATTESTATION

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.
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.


ERNESTO D. ACOSTA
Presiding Justice