

[WITH RESOLUTION OF OCT. 30, 1964]

G.R. No. 13554. February 28, 1961

Ponente: PADILLA, J.

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PADILLA, J.:

This is a petition filed by the Collector of Internal Revenue under Section 18, Republic Act No. 1125, for review of a judgment rendered on 22 January 1958 by the Court of Tax Appeals, holding that the University of the Visayas (formerly Visayan Institute) is exempt from payment of income tax under the provisions of section 27 (e) of the National Internal Revenue Code and that the assessments for income tax made by the petitioner for the years 1946 to 1950, inclusive, in the total sum of P46,592.03, exclusive of surcharges, penalties and interests are null and void, and ordering the petitioner to refund to the respondent the sum of P13,811.31 for income tax erroneously paid by the respondent (C.T.A. Cebu civil case No. R-3434).

The respondent did not file with the Bureau of Internal Revenue returns of net income for the years 1946 to 1950, inclusive. After investigation conducted by an examiner of the Bureau of Internal Revenue, the examiner filed returns of respondent's net income for the said years based upon the profit and loss statements shown and submitted to the examiner by the respondent's accountant (Exhibits 7, 7-A, 7-B, 7-C, 7-D, G, G-1, G-2, G-3, G-4). On 3 and 8 September 1951, the petitioner assessed the respondent for income received during the years 1946 to 1950, inclusive, and the tax due thereon, surcharges and penalties, computed as follows:

1946:

Net income as per return

P27,893.52

Add: Book binding disallowed

7,064.00

Net income as per investigation

P34,957.52

Tax due at 12%

4,194.90

26% surcharge

1,084.72

Total Amount Due

P5,243.62

1947:

Net income as per profit and loss statemen

P63,070.24

Add: Book binding

7,120.70

Depreciation

6,306.00

Net income as per investigation

P76,496.94

Tax due at 12%

P9,179.63

25% surcharge

2,294.90

Total Amount Due

P11,474.53

1948:

Net income as per profit and loss statement

P53,387.62

Add: Book binding

7,977.16

Depreciation disallowed

10,341.60

Net income as per investigation

P71,706.38

Tax due at 12%

8,604.77

25% surcharge

2,151.19

Total Amount Due

P10,755.96

1949:

Net income as per investigation

P109,156.06

Tax due at 12%

13,098.73

25% surcharge

3,274.68

Total Amount Due

P16,373.41

1950:

Net income per profit and loss statement

P48,971.58

Add: Depreciation disallowed

22,990.98

Total net income per investigation

P71,962.56

16% tax due

11,614.00

25% surcharge

2,878.00

Compromise

20.00

Total Amount Due

P14,412.00

(pp. 221-222, 204, BIR rec.): Assessment Nos. AR-123696-50/46, 123697-50/47, 123698-50/48, 123699-50/49 and 123700-50/50 were sent to the respondent (pp. 183, 179, 175, 172, 202, BIR rec). On 1 and 2 December 1951 the respondent sent telegrams to the petitioner requesting that it be allowed to pay the taxes, surcharges and penalties by installment at the rate of P1,000 a month (pp. 223-224, BIR rec). On 10 December 1951 the petitioner replied that the respondent could settle its obligation to the Government by paying it in twelve monthly installments at the rate of P5,808.02 per month, the first installment due and payable on or before 15 January 1952, provided that the respondent would file a surety bond on or before 10 January 1952 to ensure payment thereof (Exhibit 11, pp. 226-227 BIR rec.). On 17 December 1951 the respondent paid P1,000 on account of the tax assessed against it (Exhibits D and 12, pp. 52-53, CTA rec.; 230-231, BIR rec). On 24 January 1952 the respondent wrote a letter dated 22 January 1952 addressed to the petitioner requesting that the 25% surcharge imposed for non-payment of income tax be eliminated because its failure to file income tax returns for the years 1946 to 1950 and to pay income tax thereon was due to the honest belief that private schools were exempt from

taxation (pp. 227-228, BIR rec). On 31 January 1952 the petitioner granted the respondent's request for elimination of the 25 % surcharge and reduced to P4,603.77 the monthly installment to be paid by the respondent, provided that the first installment would be due and payable on or before 29 February 1952 and that the surety bond to insure payment would be filed by the respondent on or before the said date, 29 February 1952. The previous assessments were amended as follows:

1946 Income tax due per investigation

P4,194.90

1947 Income tax due per investigation

9,179.63

1948 Income tax due per investigation

8,604.77

1949 Income tax due per investigation

13,098.73

1950 Income tax due per investigation

11,514.00

Total

P46,592.03

6% surcharge

2,329.60

1% mo. int. from 9/30/51 to 12/17/51

1,195.86

Total amount due on 12/17/51 (w/out compromise)

P50,117.49

Less: amt. pd. on 12/17/51 under O. R. 357822

1,000.00

Balance as of 12/17/51 (w/out compromise)

P49,117.49

1% mo. int. on P46,592.03 from 12/17/51 to 1/31/53

5,987.75

Compromise for late filing (P20.00 each year)

100.00

Compromise for late payment

40.00

Total Amount Due on 1/31/53

P55,245.24

(Exhibits D and 12, pp. 52-53, CTA rec; 230-231, BIR rec). On 29 February, 3 April and 5 May 1952, the respondent paid to the City Treasurer of Cebu the monthly installment at the rate of P4,603.77, or the total sum of P13,811.31 (Exhibits A, B, C).

On 1 March 1954 the respondent wrote to the petitioner requesting that the amount of P1,000 (paid on 17 December 1951, O.R. No. 557822, see Exhibits D and 12) and P13,811.31, or a total of P14,811.31, be refunded to it on the ground that being a corporation organized and operated exclusively for educational purpose, it was exempt from the payment of income tax (p. 235, BIR rec). On the same day, 1 March 1954, the respondent brought an action against the petitioner in the Court of First Instance of Cebu for recovery of the sum of P14,811.31 (civil No. R-3434). On 7 April 1954 the petitioner filed his answer to the complaint with counterclaim. After the enactment into law of Republic Act No. 1125 on 16 June 1954, upon motion of the Assistant Provincial Fiscal, on 6 November 1954 the Court of First Instance of Cebu certified the case to the Court of Tax Appeals pursuant to the provisions of section 22, in connection with section 7, Republic Act No. 1125. After hearing, on 22 January 1954 the Court of Tax Appeals rendered judgment, the dispositive part of which is as stated at the beginning of this opinion. On 6 March 1958 the petitioner filed a notice of appeal in the Court of Tax Appeals and on 20 March 1958, within the extension of time previously granted, a petition for review in this Court.

Section 27 (e) of the National Internal Revenue Code, as amended, the provisions of law involved in the case at bar, provides:

The following organizations shall not be taxed under this Title in respect to income received by them as such—

* * * * *

(e) Corporations or associations organized and operated exclusively for religious, charitable, scientific, athletic, cultural, or educational purposes, or for the rehabilitation of veterans no part of the income of which inures to the benefit of any private stockholder or individual; Provided, however, That the income of whatever kind and character from any of its properties, real or personal, or from any activity conducted for profit, regardless of the disposition made of such income, shall be liable to the tax imposed under this Code;

A corporation or association claiming exemption from the payment of income tax as provided for in the aforequoted provision of law, must show that it is organized and operated exclusively for religious, charitable, scientific, athletic, cultural or educational purposes, or for the rehabilitation of veterans and that no part of its income inures to the benefit of any private stockholder or individual.

The petitioner claims that the respondent is a corporation organized for profit which inures to the benefit of Vicente Gullas, its president. The respondent denies the petitioner's claim.

In *Collector of Internal Revenue vs. V. G. Cinco Educational Corporation*, 100 Phil., 126; 53 Off. Gaz., 2470, the facts are: In June, 1949 Vicente G. Cinco established and operated an educational institution known as Foundation College of Dumaguete. On 21 September 1951, in view of the requirement of the Department of Education that as far as practicable, schools and colleges recognized by the government should be incorporated, Vicente G. Cinco and the members of his immediate family organized a non-stock corporation known as the V. G. Cinco Educational Institution, Inc., which was capitalized by Vicente G. Cinco and the members of his immediate family. Vicente G. Cinco acted as chairman of the board of directors and president of the college and in 1949 as a part time teacher but did not collect his salary. The college derived its income solely from the tuition fees paid by students enrolled and realized profits out of its operation but did not distribute any dividend or profit to its stockholders. Part of its income was spent in acquiring additional buildings and equipment. In upholding the corporation's claim that under the provisions of section 27 (e) of the National Internal Revenue Code, it is exempt from the payment of income tax because it is organized and maintained exclusively for educational purposes and no part of its income inures to the benefit of any individual or stockholder, this Court said:

"* * * The fact is that, as it has been established, the appellee is a non-profit institution and since its

organization it has never distributed any dividend or profit to its stockholders. Of course, part of its income went to the payment of its teachers or professors and to the other expenses of the college incident to an educational institution but none of the income has ever been channeled to the benefit of any individual stockholder. The authorities are clear to the effect that whatever payment is made to those who work for a school or college as a remuneration for their services is not considered as distribution of profit as would make the school one conducted for profit. Thus, in the case of Mayor and Common Council of Borough of Princeton vs. State Board of Taxes & Assessments, et al., 115 Atl., 342, wherein the principal officer of the school was formerly its owner and principal and as such principal he was given a salary for his services, the court held that school is not conducted for profit merely because moderate salaries were paid to the principal and to the teachers.

Of course, it is not denied that the appellee charges tuition fees and other fees for the different services it renders to the students and in fact it is its only source of income, but such fact does not in itself make the school a profit-making enterprise that would place it beyond the purview of the law. In this connection this Court made the following comment:

"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 these organizations usually have a very precarious existence. The final result of appellant's contention, if adopted, would be to discourage the establishment of the colleges in the Philippines, which is precisely the opposite of the objective consistently sought by our laws.

"Again, the amount of fees charged by a school, college or university depends, ultimately, upon the policy and a given administration, at a particular time. It is not conclusive of the purposes of the institution. Otherwise, such purpose would vary with the particular persons in charge of the administration of the organization." (Jesus Sacred Heart College vs. Collector of Internal Revenue, 95 Phil., 16.)

Another point raised by appellant to show that appellee is not entitled to the exemption of the law refers to the use made by it of part of its income in acquiring additional buildings and equipment which, it is claimed, would in the end redound to the benefit of its stockholders. Appellant claims that "by capitalizing its earnings in the aforementioned manner, the value of the properties of the corporation was enhanced and, therefore, such profits inured to the benefit of the stockholders or members. The property of the corporation may be sold at any time and the profits thereof divided among the stockholders or members."

This claim is too speculative. While the acquisition of additional facilities may redound to the benefit of the institution itself, (it) cannot be positively asserted that the same will redound to the benefit of its stockholders, for no one can predict the financial condition of the institution upon its dissolution. At any rate, it has been held by several authorities, that the mere provision for the distribution of its assets to the stockholders upon dissolution does not remove the right of an educational institution from tax exemption. Thus, in the case of U. S. vs. Pickwick Electric Membership Corp., 158 F. 2d 272, 277, it was held—"The mere fact that the members may receive some benefit on dissolution upon distribution of the assets is a contingency too remote to have any material bearing upon the question where the association is admittedly not a scheme to avoid taxation and its good faith and honesty of purpose is not challenged." (100 Phil., 133-135; 53 Off. Gaz. pp. 2473-2475.)

Sometime in 1919, Vicente Gullas established a school in Cebu City known as the "Visayan Institute" and for a few years remained its sole owner. On 1 October 1921 Vicente Gullas, Pantaleon E. del Rosario, Paulino Gullas, Manuel C. Briones and Eugenio S. del Rosario formed a non-stock corporation with an authorized capital of P20,000 for the purpose of (establishing and maintaining a school to be named as the "Visayan Institute" [(Exhibits 1, 1-A. pp. 193 (i) to 198 (k)]. The plan was to finance the school by selling to the public bonds with a par value of P100 each payable out of the funds of the corporation and the interests to be fixed by the by-laws. However, the financing plan was abandoned and instead of selling bonds to the public, Vicente Gullas and his wife "put in" their "own money." On 29 August 1930 the Visayan Institute amended its articles of incorporation by converting it into a stock corporation with an authorized capital of P50,000, subscribed and paid as follows by:

Name

No. of Stocks

Subscribed

Amount paid

Pantaleon E. del Rosario

70

7,000

Eugenio S. del Rosario

70

7,000

Manuel C. Briones

70

7,000

Paulino Gullas

70

7,000

Vicente Gullas

220

22,000

According to the amended articles of incorporation, all shares of the corporation had been subscribed and paid for (Exhibits 2, 2-A, E, E-2, pp. 193 (f) to 193 [h]). In March 1948 the Visayan Institute was raised to the category of a university and renamed "University of the Visayas."

Vicente Gullas, president of the respondent, testified that the respondent is not engaged in a profit-making enterprises but in a purely educational pursuit; that the sources of income of the respondent are the various fees paid by the students like annual fee, book rental, etc.; that these receipts are spent for salaries of teachers, repair of the buildings, purchase of library books and athletic equipment, scholarship, funds and contributions to charity; that while the respondent realizes profit out of its operation, the profit goes to the improvement and repair of the buildings, purchase of library books and equipment, establishments of scholarship funds and purchase of musical instruments; that since its original incorporation, no dividends have been declared and distributed to the stockholders; and that as president of the respondent, he receives a salary of P1,000 a month and P300 a month allowance for transportation, representation and entertainment.

Teofilo Castillejo, accountant of the respondent, testified that the income of the respondent is derived only from admission, tuition, diploma, ROTC and laboratory fees paid by the students; that no dividends have been distributed to its stockholders since its incorporation; and that the net income of the respondent remains as surplus in its book of accounts.

Juan Gandiongco, at present chief of the Collection Branch, BIR Regional District No. 7, and from 1934 to the end of the war and from 1946 to 1951, was an income tax examiner, testified that sometime in 1941 he examined the books of account of the Visayan Institute and submitted a report of his examination to the chief of the Income Tax Division; and that in the course of his examination of its books of account, he found that at no time from 1920 to 1941 did the Visayan Institute declare any stock or cash dividend.

Zacarias Chua, Group Supervisor in the Bureau of Internal Revenue and income tax examiner, and from 1946 to 1951 was stationed in Cebu City, testified that in 1951 he had occasion to examine the books of account of the Visayan Institute or the University of the Visayas; and that he did not find any declaration and payment of cash dividend to its stockholders.

At present, the stockholders of the corporation and their respective shareholding and investment are:

Name

No. of Shares

Amount

1.

Atty. Vicente Gullas

200

P20,000.00

2.

Atty. & Mrs. Vicente Gullas

90

9,000.00

3.

Senator Manuel C. Briones

65

6,500.00

4.

Atty. Vicente del Rosario

30

3,000.00

5.

Dr. Rosario Gullas-Cruz

30

3,000.00

6.

Atty. Braulio K. Oro and Alberto Pusod

5

500.00

7.

Mr. Jose E. Gullas

15

1,500.00

8.

Mr. Eduardo R. Gullas

15

1,500.00

9.

Miss Glicoria R. Gullas

15

1,500.00

10.

Mrs. Josefina R. Gullas

15

1,500.00

11.

Mr. Felicisimo Cabusas

5

500.00

12.

Pres. U. V. Alumni Association

5

500.00

13.

Atty. Hipolito Alo

5

500.00

14.

Mr. Sabas Ramirez

5

500.00

50,000.00

(Exhibit 15, p. 310, BIR rec). The following is a list of stockholders employed by and receiving compensation from the respondent:

Year 1946

1.

Atty. Vicente Gullas, President

P3,000 July to
December 1946

2.

Dr. Rosano G. Cruz, Secretary

750 July to
December 1946

Year 1947

1.

Atty. Vicente Gullas, President

P6,000 Jan. to
December 1947

2.

Dr. Rosario G. Cruz, Secretary

1,200 Jan. to
December 1947

3.

Mrs. Josefina K. Gullas, Treasurer

650 Jan. to
December 1947

Year 1948

1.

Atty. Vicente Gullas, President

P6,600 Jan. to
December 1948

2.

Mrs. Josefina E. Gullas, Treasurer

2,421 Jan. to
December 1948

3.

Dr. Rosario G. Cruz, Secretary

1,200 Jan. to
December 1948

Year 1949

1.

Atty. Vicente Gullas, President

P13,000 Jan. to
December 1949

2.

Mrs. Josefina E. Gullas, Treasurer

3,000 Jan. to
December 1949

3.

Hon. Vicente del Rosario, Instructor

375 Jan. to
December 1949

Year 1950

1.

Atty. Vicente Gullas, President

P12,000 Jan. to
December 1950

2.

Mrs. Josefina K. Gullas, Treasurer

4,200 Jan. to
December 1950

(Exhibit 16, p. 290, BIR rec.) .

The respondent has satisfactorily established its claim that it is organized and operated, exclusively for educational purposes and that no part of its income has inured to the benefit of any stockholder or individual. The original articles of incorporation of the respondents states—

That the purpose for which such, corporation is formed for the upbuilding and development of the mind and body of the Filipino youth, and to promote that which is helpful and beneficial to the moulding of their character. To accomplish this end, the corporation shall establish and maintain, to begin with, a high school course, a school of law and of commerce, and may also establish sometime in the future some other institutions of learning such as colleges of education, medicine, engineering etc. (Exhibit 1)

and its amended articles of incorporation states—

That the purpose for which such corporation is formed is to give to the Filipino youth such training and instruction which may make them well-prepared to honorably exercise the rights and to perform and discharge the duties and obligations of a good, patriotic and useful citizen. The corporation will direct its efforts to the symmetrical development of their character, mind and body. To accomplish this end, the corporation will establish and maintain, to begin with, a high school or secondary course of instruction, a college of commerce and business administration, and a college of law: In the future, when conditions warrant it, the corporation may open, establish and maintain additional courses, schools, and colleges, such as: college of liberal arts, college of education, college of engineering, college of dentistry and pharmacy, college of medicine And surgery, et al., (Exhibit E-1).

The above quoted purposes of the respondent show that it is engaged in an educational endeavor and in no other. The profit and loss statements of the respondent for the years 1946 to 1950, inclusive, show that its income was solely derived from admission fees, tuition fees, diploma fees, graduation fees, ROTC fees and laboratory fees paid by the students (Exhibits G, G-1, G-2, G-3, G-4).

The fact that the original articles of incorporation was amended to convert the corporation from a non-stock to a stock corporation is not a conclusive proof that the respondent is engaged in a profit-making business, part of which inures to the benefit of a single stockholder or individual. As correctly held by the Court of Tax Appeals, "Section 27 (e) of the National Internal Revenue Code does not make any distinction between stock and non-stock corporations, and it is not for this Court to make the distinction."

The fact that when on 29 August 1930 the corporation was converted from a non-stock to a stock corporation, "its assets had increased from P6,000.00 cash and P3,000.00 worth of books (t.s.n., p. 23) into assets worth P50,000.00, which were distributed in the form of shares of stock to the members of the non-stock corporation, predecessor of the stock corporation (Exhibit 2, p. 13 h, Vol. I, BIR rec.);" and that at the meeting of the Board of Trustees of the respondent held on 12 February 1950, there was a move to double the stock dividend of the

corporation "in view of P200,000 gain in property—real and personal besides the goodwill," which was not actually carried out (Exhibits 3-B, 3-C, p. 39, BIR rec), is not enough for an inference that the respondent has been turned into a corporation for business and profit. The fact is that since its incorporation, the respondent has not declared any cash dividend and no part of its profits has inured to the benefit of any stockholder or individual. The mere realization of profits out of its operation does not automatically result in the loss of its privilege of exemption from the payment of income tax as long as no part of the profits inures to the benefit of any stockholder or individual.

The petitioner's claim that the respondent has invested in other schools established in Toledo, Danao, Sogod, Colon, Sibonga and Cebu City is denied by Vicente Gullas, president of the respondent, who testified that the respondent is merely supervising these schools and does not receive any fee for such; that the only benefit the respondent derives in return is the encouragement of the graduates of the supervised schools to enroll in the respondent; that it is the witness himself who supervises them and receives remuneration for his services and not the respondent, and that although at the meeting of the board of trustees of the respondent held on 12 February 1950, there was a move to require the Toledo Colleges, Danao Colleges and Cebu Northern High Schools to give the respondent 5% of their admission fees and 10% of their graduation fees as remuneration for checking their financial account and for advertising their schools, yet the board of trustees had not been able to compel them to do so because the supervised schools stood "on their own and not directed by the University of the Visayas" and that "they pay directly their fees to Manila or they cannot get graduation special order or when there is a contribution for girl scouts or boy scouts or for the anti T.B., they don't pay thru the University of the Visayas."

Neither the fact that there was an offer to purchase the assets of the University of the Visayas for the sum of P4,000,000, which means that the stockholder's original investment of P1 is now worth P119, nor that fact that the respondent's profits are being kept for future distribution to stockholders would deprive the respondent to the privilege of exemption. As long as it continues to engage solely in the operation and maintenance of the school and no dividend inures to the benefit of any stockholder or individual, the respondent would enjoy the exemption from the payment of income tax provided for in section 27 (e) of the National Internal Revenue Code.

The action for refund, as far as the sum of P1,000 paid by the respondent on 17 December 1951 is concerned, is already barred.[1] The respondent does not insist on asking for refund of this sum. And as far as the action for refund of the sum of P4,603.77 paid by the respondent on 29 February 1952 is concerned, the Court of Tax Appeals correctly ruled that it is not barred, because as the last day of the two-year period (28 February 1954) within which an action may be brought in court for its refund, as provided for in section S06 of the National Internal Revenue Code, fell on Sunday, the action for refund brought by the respondent in the Court of First Instance of Cebu on the following day, to wit: 1 March 1954, was within the statutory period. The action for refund of P4,603.77 paid on 3 April, and of an equal amount paid on 5 May 1952, by the respondent, is obviously within the statutory period.

The judgment under review is affirmed, without pronouncement as to costs.

Bengzon, Acting C. J., Bautista Angelo, Labrador, Concepcion, Reyes, J. B. L., Barrera, Paredes and Dizon, JJ., concur.

[1] Section 306, National Internal Revenue Code, Commonwealth Act No. 466.

RESOLUTION

October 30, 1964

REYES, J. B. L., J.:

The Commissioner of Internal Revenue has moved for the reconsideration of our decision in the above-entitled case affirming the decision of the Court of Tax Appeals in its interpretation and application of Section 27 (e) of the tax code, and declaring: (1) that appellee University of the Visayas be exempt from income tax under Section 27(e) of the Internal Revenue Code; (2) annulling the income tax assessments for 1946 to 1950 made against the University; and (3) ordering the refund of previous income taxes collected from it.

The petitioner-movant re-asserts his position that the respondent University of the Visayas is not tax-exempt because the legislature intended to remove from the purview of the exemption provided for in Section 27 (e) of the Revenue Code not only organizations or corporations distributing cash dividends to any stockholder or individual but also those whose income inures to the benefit of any stockholder or individual. In support thereof, he emphasizes the difference between the old law (Commonwealth Act No. 466) thus:

"(f) Corporation or association organized and operated exclusively for religious, charitable, scientific, athletic, cultural, or educational purposes, no part of the net income of which is distributed to any private stockholder or individual:

and its amendment by Republic Act No. 82, as follows:

"(c) Corporation or association organized and operated exclusively for religious, charitable, scientific, athletic, cultural or educational, purposes, or for the rehabilitation of veterans no part of the net income of which inures to the benefit of any private stockholder or individual * * *."

and finally cites and relies on the explanatory note to House Bill No. 729, which became Republic Act No. 82. The pertinent portions of the explanatory note are hereunder quoted:

"The attached bill, therefore, proposes to increase the present rates of income tax and to modify the other features of the present law "with a view of providing additional revenue. A brief explanation of the changes proposed to Title II (Income Tax) of the National Internal Revenue Code is set forth below.

"4. Amendment of provision granting exemption in favor of religious, charitable, scientific, athletic, cultural, or educational organizations or institutions. The present law section 27(f), National Internal Revenue Code exempts the organizations if no part of their net income "is distributed to any private stockholder or individual." This provision has been authoritatively construed as exempting such organization or association from payment of the income tax for any year in which no dividends are distributed to stockholders. The present law as so construed, therefore, makes it possible for a corporation to avoid the payment of income tax by simply desisting from declaring a divider during any given year notwithstanding the fact that it may have earned a very substantial amount of income in that year. Furthermore, if the corporation desires to distribute dividends, it could effect the distribution during a taxable year in which it expects to suffer a loss, or derive only a small income, thus making it possible for such corporation to entirely avoid the payment of the income tax by availing of the loophole in the law to suit its advantage. Under the proposed amendment, the above-mentioned corporations and associations will pay income tax on their profits in any year although no dividends are declared for such year." (Congressional Record, House of Representatives, Sept. 9, 1946, Vol. 1, No. 69, p. 1599.)

The Revenue Commissioner further argues that the undistributed dividends necessarily increase the value of the stockholders' equity, and that, in the particular case, it is not denied that the market value of the shares of the University of the Visayas has increased considerably; hence, it is urged, the undistributed dividends actually

inured to the benefit of its private stockholders, thus coming within the purview of the statutory requisite for taxability.

In reply, the appellee University of the Visayas argues that the foregoing explanatory note lends no assistance to the movant's position because it merely states the intended safeguard or remedy against tax evasion without, however, expressing that the intent of the legislature was to withdraw the exemption from income tax of the corporations or institutions enumerated in Section 27 (e). The law itself, it is argued, sanctions the exemption; and if the exemption were withdrawn, the law would have simply taxed educational institutions that produce a net income or profits. Appellee further urges that, literally understood, the said Section 27 (e) would tax all the institutions mentioned therein that have any net income whatever, since the production of net income naturally (although not necessarily) results in the increase of the stockholders' equity in the corporation; but such a literal interpretation has no justification, and would make the law senseless in its application by granting and, at the same time, withdrawing the exemption.

Finally, appellee argues that under the interpretation advocated by the Revenue Commissioner, only educational institutions without net income would be exempt; and that the increase of a stockholder's equity in the corporation is not only theoretical while the shares are not disposed of, or the corporation liquidated, but may arise from causes unconnected with its net income. That what is referred to by the phrase "net income inures to the benefit of any private stockholder or individual" is the disposition or channeling of the net income of the corporation to the benefit of the stockholder or individual in an indirect or manipulative manner.

We have carefully reexamined the records of this case, and reached the conclusion that while the arguments advanced by the appellee educational institution are deserving of careful consideration and bear weight, the peculiar circumstances of the present case clearly indicate that said original appellee is not entitled to claim exemption, contrary to our original decision. The reason is that the facts of record prove that the corporation is under absolute control of the president and his immediate family (who hold 85% of the capital stock) to an extent that warrants the conclusion that the corporate entity is but an alter ego or a business conduit for said stockholders; wherefore, a disregard of the corporate fiction is justified, and the net income of the corporation may well be viewed as that of the controlling group (cf. *Koppel [Phil.] Inc. vs. Yatco*, 77 Phil., 496, and authorities cited).

The operation of the appellee educational enterprise was indeed limited to educational purposes, and the income derived solely from admission, tuition, diploma, laboratory and ROTC fees paid by students. However, the net income of P302,479.02 from 1946 to 1950, with the exception of the relatively small amount of P28,000 intended for operating expenses, were invested in the purchase of real properties. Said properties, it is admitted, belong to the university, but they have been placed in the name of the president alone, or in the name of his wife, or both. The reason is that, as the president truthfully admitted, he is the university and the university belongs to him. Shares of stock belonging to other stockholders were acquired by the president, and although not at their market value, nevertheless, at prices very much more than par value. No less than the president testified that for every peso share the value is now P119. This increase in value is due not only to the operation of the educational enterprise but also in the increase of its permanent assets, including those that had been placed in the name of the president, his wife, or both. One of the facts clearly denoting that the personality of the university and that of the president is one is that the board of directors of the university had once proposed the issuance of additional shares on the accumulated net income or profits. The president, however, objected to this proposal of the majority of the persons composing the board for the reason that the same would be a useless and unnecessary gesture, as he was practically the corporation. The objection of the president defeated the proposal.

Considering that the net income, except for the sum of P28,000.00 set aside for operational expenses, was

invested in permanent assets placed in the name of the president, his wife, or both, it is very obvious that such net income realized by the university inured to the benefit of the president and his family. It is thus perfectly understandable that the president would decline to declare dividends. Having the permanent assets consisting of seven buildings in his name or that of his wife, he is certainly benefited by desisting from declaring any kind of dividend. If dividends had been declared and distributed the funds and assets of the university would be diminished, insofar as the president and his family is concerned, to the amount, although insignificant, that has to be distributed to the stockholders holding 15% of the shares. However, if no dividends are declared or distributed, 100% of the net income or accumulated funds or assets of the corporation would remain with him, so that he would benefit not only from his 85% holding but also from the 15% holding of others.

The foregoing proves in a clear manner, not only on the basis of a statement under oath but also on the history of the respondent institution from incipency to the present time when the tax is being collected, the existence of a setup designed to avoid the payment of taxes. If the net income of the institution inured to the benefit of the university, as claimed by its president under the aforementioned circumstances, it likewise inured to the benefit of the president, as the two are admittedly, and shown to be, the same. Hence, the university is liable for income tax under the amendment.

In view of the foregoing considerations, the original decision of 28 February 1961 is hereby reconsidered and set aside, and another one entered (a) reversing the decision of the Court of Tax Appeals, in CTA Cebu CM Case No. R-3434, and declaring appellee University of the Visayas not entitled to the refund of P13,811.31, for income taxes previously paid; (b) denying the refund aforesaid; (c) declaring that the Commissioner of Internal Revenue was lawfully empowered to assess and collect income taxes from the appellee, University of the Visayas; and (d) ordering the said appellee to pay the amount of P37,212.06, as taxes on its income for the years 1946 to 1950, together with one per centum (1%) monthly interest on the sum of P31,780.72 until paid, plus the sums of P40 and P100 as administrative penalties for lateness in filing returns and payment. No costs.

Concepcion, Barrera, Paredes, Dizon, Regala, Makalintal, Bengzon, and Zaldivar, JJ., concur.

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