

## **EXPLANATORY NOTE**

Under the 1987 Constitution, the State is mandated to give priority to education as a means to accelerate social progress, and promote total human liberation and development, through the constitutional guarantee of the right to quality education at all levels, and the accessibility of education for all,<sup>1</sup> and recognizes “the complementary roles of public and private institutions in the educational system,”<sup>2</sup> and pursuant thereto grants, among other things, that “All revenues and assets of non-stock, non-profit educational institutions used actually, directly, and exclusively for educational purposes shall be exempt from taxes and duties. . . . Proprietary educational institutions, including those cooperatively owned, may likewise be entitled to such exemptions subject to the limitations provided by law including restrictions on dividends and provisions for reinvestment.”<sup>3</sup>

However, various regulatory bodies and agencies of the government have conflicting positions as regards tax impositions, which are not only confusing but sometimes even in contravention of the Constitutional exemptions. One such instance is the BIR requirement that a non-stock non-profit educational institution should file an application for qualification and to secure a certificate of exemption before enjoying the said tax exemption.<sup>4</sup> This has no legal basis, inasmuch as the constitutional tax exemptions given to non-stock non-profit educational institutions are self-executory and immediately enforceable without need of enabling legislation.<sup>5</sup>

By express constitutional provision, the test of exemption from taxation is the use of the property for purposes mentioned in the Constitution. The exemption extends to facilities which are incidental to and reasonably necessary for the accomplishment of the main purposes.<sup>6</sup> Such property may not be used for commercial purposes. Moreover, the phrase “exempt from taxation” should not be interpreted to mean exemption from all kinds of taxes.<sup>7</sup> The sale of real property owned by the educational institution is subject to transfer tax and documentary stamp tax, inasmuch as this is an activity which is not related to education but is assumed to be done for profit. This is also the same reason given for the imposition of income tax on rent income to commercial entities (e.g., banks or concessionaires) from real property.

Moreover, it is clear under the Constitution that educational institutions shall not be subject to tax for revenues and assets used actually directly and exclusively for educational purposes. However, they shall be subject to internal revenue taxes on income from trade, business or other activity, the conduct of which is not related to the exercise or performance by such educational institutions of their educational purposes

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<sup>1</sup>Sec. 1, Article XIV of the 1987 Constitution.

<sup>2</sup>Sec. 4(1), Article XIV of the 1987 Constitution.

<sup>3</sup>Sec. 4(3), Article XIV of the 1987 Constitution.

<sup>4</sup> See: Revenue Memorandum Circular No. 14-2001 (12 March 2001) attached below.

<sup>5</sup> Sarmiento, Ulpiano. Education Law 2009 ed., p. 845 (School Finance: Policy).

<sup>6</sup> Apostolic Prefect v. City Treasurer of Baguio, 71 Phil, 547 [1941]

<sup>7</sup> Rev. Fr. Casimiro Llado vs. The Commissioner of Internal Revenue, 14 SCRA 292 (19\*\*).

or function.<sup>8</sup> In addition, interest income from Philippines currency bank deposits and yield from deposit substitute instruments used actually, directly and exclusively in pursuance of its purpose as an educational institution, are exempt from the 20% final tax imposed by Sec. 24(e)(l) of the Tax Code, as amended.<sup>9</sup> It should be noted, however, that the tax exemption granted under this provision does not cover withholding taxes.<sup>10</sup>

At present, the BIR imposes income tax on the basis of the source of income. So therefore, if the school had earned income from an activity which is solely educational in purpose, then this is considered exempt. On the other hand, if the income is earned from a purely commercial activity, then this is an activity not actually, directly and exclusively for educational purposes, and hence, taxed.

If the State is truly committed to education as the best weapon against poverty and accelerate social progress, then it may consider the creation of additional incentives (such as expanded tax exemptions) to educational institutions as the Government's counterpart investment (or subsidy) in its drive to make quality education accessible to all. There is a need to clarify and further augment the tax exemptions granted to educational institutions in order to achieve the constitutional precepts.

The bill therefore seeks to achieve the following objectives:

*First*, to clarify and make absolute the constitutional exemptions:

- (a) from income tax, capital gains tax, and all other internal revenue taxes, as the case may be, all income, receipts and earnings of educational institutions realized or arising from pursuing their educational objectives;
- (b) from tariffs and duties all properties of educational institutions imported from abroad, which are to be used and employed in pursuing their educational objectives, and that in the event of subsequent sale or disposition of said properties, the same would also be exempt from all income tax, capital gains tax, and all other internal revenue taxes, as the case may be;
- (c) from real property taxes all the real properties and improvements therein used or intended for use, if idle, in the pursuit of their educational objectives, including the grant of scholarships to poor and deserving students.

*Second*, to expand such exemptions as follows:

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<sup>8</sup> Sec. 2, Finance Department Order No. 137-87, as amended by Finance Department Order No. 92-88

<sup>9</sup> Finance Department Order No. 149-95

<sup>10</sup> Letter-opinion dated 13 March 1996 from LiwaywayVinzons-Chato, Commissioner, Bureau of Internal Revenue (BIR) to Dr. Angel C. Alcala, Chairman, Commissioner of Higher Education (CHED)

- (a) to exempt from income tax, capital gains, tax, and all other internal revenue taxes, as the case may be, all income receipts and earnings of educational institutions realized or arising from pursuing ancillary or allied undertakings which are incidental to, necessary or supportive of meeting their educational objectives, such as the operation of cafeterias, canteens, bookstores, parking facilities, business processing outlets, internet cafes, printing and publishing outlets, etc., provided, the income, receipts or earnings are devoted in pursuance of the educational objectives of the educational institution;
- (b) to exempt from tariff or duties all properties of educational institutions which they import from abroad to be used for such ancillary undertakings, and that in the event of subsequent sale or disposition of said properties, the same would also be exempt from all income tax, capital gains tax, and all other internal revenue taxes, as the case may be;
- (c) to exempt from all forms of real property taxes all real properties and improvements therein of educational institutions which are used in the pursuit of ancillary or allied services, provided that the profits or earnings therefrom are devoted exclusively for the pursuit of educational objectives, particularly the grant of scholarships to poor and deserving students; and
- (d) to exempt from income tax, withholding tax, capital gains tax, value added tax and all other forms of internal revenue taxes, as the case may be, the sale, exchange, transfer or disposition of such real properties and improvements therein.

## **AN ACT AFFIRMING, CLARIFYING, AND ENHANCING, THE EXEMPTION OF EDUCATIONAL INSTITUTIONS FROM TAXES AND DUTIES**

SECTION 1. This Act shall be known as “*The Comprehensive Tax and Duty Exemption for Educational Institutions Act.*”

SEC. 2. *Declaration of Basic Policy* - It is the policy of the State to establish and maintain a complete, adequate and integrated system of education relevant to the goals of national development. Toward this end, the State should clarify and enhance the tax and duty exemptions enjoyed by educational institutions under the Constitution, but should provide and expand such exceptions, and thereby provide a comprehensive tax and duty exemption system for educational institutions to ensure their financial viability in pursuing in partnership with the government the maximum contribution of the educational system to the attainment of the national developmental goals.

SEC. 3. *Definition of Terms.* – The following terms as used in this Act shall be defined as follows:

“*Educational institution*” means any school or institution duly recognized by the Department of Education (DepEd), Commission on Higher Education (CHED), or the Technical Education and Skills Development Authority (TESDA), which undertakes educational or training objectives, in accordance with existing laws and regulations.<sup>11</sup>

“*Proprietary educational institution*” is any educational institution maintained and administered by private individuals or groups.

“*Nonstock and nonprofit education institution*” is any educational institution maintained and administer by private individuals or groups which does not allow for the distribution of dividends or profits to its members, officers, directors or trustees.

“*Allied activities*” pertains to any and all undertakings, projects and activities of an educational institution, which is not directly in pursuit of its educational objectives, but which are necessary, incidental, complementary or supportive of meeting the educational institution’s educational objectives, such as, but not limited to opening and maintaining any and all forms of currency banks deposits, investments in securities and in deposit substitute instruments, operating canteens, cafeterias, book stores, internet cafes, printing and publishing, business centres, and parking facilities, even when conducted for profit by such educational institution within their premises, whenever the same is allied to or incidental to undertaking their educational objectives; the leasing out of commercial spaces within their premises to commercial merchants who are able to offer their facilities and services to the student, faculty and employees of the educational institution, even when such facilities are also available to the public, shall be considered as allied activities; *Provided, however,* that all profits and earnings from such allied activities are used directly and exclusively by the educational institution towards achieving its educational objectives, including the granting of scholarships to poor and deserving students.

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<sup>11</sup>Adopted from Sec. 27(B), 1997 NIRC.

SEC. 4. – *Comprehensive Exemption from Income Tax.* – Notwithstanding any provision in the National Internal Revenue Code or in any other statute to the contrary, a nonstock and nonprofit educational institution shall be exempt from income tax in respect to income received by nonprofit and nonstock educational institution, including income of whatever kind and character from any of their properties, real or personal, or from any of their activities as an educational institution, including allied activities Provided, however that all such income are disposed for their furtherance of their primary purpose as an education institution.

SEC. 5. – *Comprehensive Exemption from Value-Added Tax and Other Internal Revenue Tax.* – Notwithstanding any provision in the National Internal Revenue Code or in any other statute to the contrary, the income, receipts or earnings of every educational institution shall be exempt from value-added taxes and any other internal revenue taxes in respect to income, receipts or earnings, of whatever kind and character, including those arising from any of their properties, real or personal, or from any of their activities conducted for profit, but allied to or incidental to undertaking their educational objectives; Provided, however, that all such income, receipt or earnings are disposed for their furtherance of their primary purpose as an education institution.

SEC. 6. – *Comprehensive Exemption from Income Tax.* – Notwithstanding any provision in the Tariff and Customs Code or in any other statute to the contrary, an educational institution shall be exempt from customs duties and tariff of all kind in respect to all importations of properties, real or personal, of whatever kind and nature into Philippine territory for purposes of being used in the pursuit of its educational objectives, including those allied activities; Provided, however, that any and all income, receipts or earnings derived from such properties shall be used exclusively for the furtherance of its principal objectives as an educational institution.

SEC. 7. – *Comprehensive Exemption from Realty Property Tax.* – Notwithstanding any provision in the Real Property Tax Code or in any other statute, ruling or ordinance to the contrary, every education institution shall be exempt from any and all real property taxes imposed or that may be imposed under any name or classification on all its real properties and all improvements therein directly used or intended for educational purpose, including all properties which are being devoted to ancillary activities; Provided, however, that all such income, receipt or earnings are disposed for their furtherance of their primary purpose as an education institution.

The sale, transfer, exchange, disposition or lease of a real properties and improvements therein by a nonstock and non-profit educational institution shall be exempt from income, value-added and other internal revenue taxes as provided in the previous sections of this Act; Provided, however, that any and all income, receipts or earnings derived from such properties shall be used exclusively for the furtherance of its principal objectives as an educational institution.

SEC. 8. *Rule-making Authority* - The Department of Finance, in coordination with the Department of Education, Commission on Higher Education, Technical Training and

Skills Development Authority (TESDA), shall promulgate the necessary implementing rules and regulations.

SEC. 9. *Separability Provision* - Any part or provision of this Act which may held invalid or unconstitutional shall not affect its remaining parts of provisions.

SEC. 10. *Repealing Clause* - All laws or parts thereof inconsistent with any provision of this Act shall be deemed repealed or modified, as the case may be.

SEC. 11. *Effectivity* - This Act shall take effect within fifteen (15) days from the date of its publication in a newspaper of general circulation.