REPUBLIC OF THE PHILIPPINES
DEPARTMENT OF FINANCE
BUREAU OF INTERNAL REVENUE

Quezon City

Sec. 39 (A), Tax Code of 1997, as amended	000-00 OT - 311 - 2022	

Person to Contact: Chief, Law & Legislative Division
Tel No.: 926-55-36/927-09-63

Date: JUN 24 2022

MR. BENITO AGUILAR

Dear Mr. Aguilar

This refers to your request for a ruling that the house and lot which you initially acquired with the intention of using such property for residential purposes is considered as capital asset and the subsequent sale of such property is exempt from the imposition of income tax, creditable withholding tax (CWT) and value-added tax (VAT).

As represented, you acquired a lot located at , ("Subject Property") in 2020. You intended to renovate the existing old, dilapidated house and use it for your own residential purposes only. Although you are engaged in leasing a single property, which business is registered with the Bureau of Internal Revenue, the Subject Property did not become part of, or used in any of your business trade. The said property was not also occupied nor tenanted or rented out from the date of purchase up to the date of sale. Due to the economic effect of the pandemic to your finances, you were constrained to sell the Subject Property in January 2021.

In reply, please be informed that Section 39 (A) of the National Internal Revenue Code (Tax Code) of 1997, as amended, provides for the definition of a capital asset, as follows:

"*Section 39. Capital Gains and Losses. —*

(A) Definitions. — As used in this Title —

(1) Capital Assets. — The term 'capital assets' means property held by the taxpayer (whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory

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of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, or property used in the trade or business, of a character which is subject to the allowance for depreciation provided in Subsection (F) of Section 34; or real property used in trade or business of the taxpayer."

The foregoing provision is being implemented by Revenue Regulations (RR) No. 7-2003, issued on February 11, 2003, providing for the guidelines in the determination of whether a particular real property is a capital asset or an ordinary asset. Sections 2 and 3 of RR 7-2003 defines capital assets and what constitutes ordinary assets as follows:

> "SECTION 2. Definition Of Terms. — For purposes of these Regulations, the following terms shall be defined as follows:
>
> a. Capital assets shall refer to all real properties held by a taxpayer, whether or not connected with his trade or business, and which are not included among the real properties considered as ordinary assets under Sec. 39(A)(1) of the Code.
>
> b. Ordinary assets shall refer to all real properties specifically excluded from the definition of capital assets under Sec. 39(A)(1) of the Code, namely:
>
>   1. Stock in trade of a taxpayer or other real property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year; or
>   2. Real property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business; or
>   3. Real property used in trade or business (i.e., buildings and/or improvements) of a character which is subject to the allowance for depreciation provided for under Sec. 34(F) of the Code; or
>   4. Real property used in trade or business of the taxpayer.
>
> xxx xxx xxx
>
> c. Real property shall have the same meaning attributed to that term under Article 415 of Republic Act No. 386, otherwise known as the "Civil Code of the Philippines."
>
> d. Real estate dealer shall refer to any person engaged in the business of buying and selling or exchanging real properties on his own account as a principal and holding himself out as a full or part-time dealer in real estate.

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e. Real estate developer shall refer to any person engaged in the business of developing real properties into subdivisions, or building houses on subdivided lots, or constructing residential or commercial units, townhouses and other similar units for his own account and offering them for sale or lease.

f. Real estate lessor shall refer to any person engaged in the business of leasing or renting real properties on his own account as a principal and holding himself out as lessor of real properties being rented out or offered for rent.

g. Taxpayers engaged in the real estate business shall refer collectively to real estate dealers, real estate developers, and/or real estate lessors. Conversely, the term "taxpayers not engaged in the real estate business" shall refer to persons other than real estate dealers, real estate developers and/or real estate lessors. A taxpayer whose primary purpose of engaging in business, or whose Articles of Incorporation states that its primary purpose is to engage in the real estate business shall be deemed to be engaged in the real estate business for purposes of these Regulations.

SECTION 3. Guidelines in Determining Whether a Particular Real Property is a Capital Asset or Ordinary Asset. —

a. Taxpayers engaged in the real estate business. — Real property shall be classified with respect to taxpayers engaged in the real estate business as follows:

1. Real Estate Dealer. — All real properties acquired by the real estate dealer shall be considered as ordinary assets.

2. Real estate Developer. — All real properties acquired by the real estate developer, whether developed or undeveloped as of the time of acquisition, and all real properties which are held by the real estate developer primarily for sale or for lease to customers in the ordinary course of his trade or business or which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year and all real properties used in the trade or business, whether in the form of land, building, or other improvements, shall be considered as ordinary assets.

3. <u>Real Estate Lessor. — All real properties of the real estate lessor, whether land and/or improvements, which are for lease/rent or being offered for lease/rent, or otherwise for use or being used in the trade or business shall likewise be considered as ordinary assets.</u>

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4. Taxpayers habitually engaged in the real estate business. — All real properties acquired in the course of trade or business by a taxpayer habitually engaged in the sale of real estate shall be considered as ordinary assets. Registration with the HLURB or HUDCC as a real estate dealer or developer shall be sufficient for a taxpayer to be considered as habitually engaged in the sale of real estate. If the taxpayer is not registered with the HLURB or HUDCC as a real estate dealer or developer, he/it may nevertheless be deemed to be engaged in the real estate business through the establishment of substantial relevant evidence (such as consummation during the preceding year of at least six (6) taxable real estate sale transactions, regardless of amount; registration as habitually engaged in real estate business with the Local Government Unit or the Bureau of Internal Revenue, etc.). (Underscoring supplied)

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Based on the foregoing, all real properties of a real estate lessor, which are for lease/rent or being offered for lease/rent, or otherwise for use or being used in the trade or business shall be considered as ordinary assets. In the instant case, the Subject Property previously intended for your residence is classified as capital asset since the said property is not for lease/rent or being offered for lease/rent, or otherwise for use or being used in your trade or business. Hence, its subsequent sale is not subject to CWT and VAT.

This ruling is being issued on the basis of the foregoing facts as represented. However, if upon investigation, it will be ascertained that the facts are different, then this ruling shall be considered null and void.

Very truly yours,

CAESAR R. DULAY
Commissioner of Internal Revenue

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