REPUBLIC OF THE PHILIPPINES
DEPARTMENT OF FINANCE
BUREAU OF INTERNAL REVENUE
Quezon City

27(D)(5); 39(A)(1); RR No. 7-2003
BIR Ruling No. 014-03; BIR Ruling No. 634-17; BIR Ruling No. 480-17; BIR Ruling No. 187-17; VAT-0404-2020
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PHILIPPINE AIRLINES, INC.
PNB Financial Center
Pres, Diosdado Macapagal Ave.
CCP Complex, Pasay City

Attention: **Mr. Gilbert F. Santa Maria**
President & CEO

Gentlemen:

This refers to your letter dated October 23, 2020 requesting for confirmation that the sale of real properties owned by Philippine Airlines, Inc. ("PAL" for brevity) and being held for investment purposes is subject to the 6% capital gains tax (CGT) and the documentary stamp tax (DST) on conveyance of real property and exempt from the value-added tax (VAT).

Background:

PAL is a domestic corporation duly registered with the Securities and Exchange Commission (SEC) with Company Reg. No. [redacted] It was also registered with the Bureau of Internal Revenue (BIR) with TIN No. [redacted] under Line of Business Nos. [redacted] as international air passenger transport and [redacted] as domestic air passenger transport.

The purposes for which PAL was formed are "to engage in transport services for the transportation of passengers, express parcels, mail merchandise and freight by air, and all other services of a similar character which may from time to time be deemed advisable, to establish, purchase, own, acquire, operate and generally turn to account, airlines, operates aerial taxi, aerial advertising and sightseeing services, to own, purchase, construct, lease, operate and dispose of airports, hangars, transportation depots, aircraft service stations and agencies, and other objects and service of a similar nature which may be necessary, convenient or useful as an auxiliary to its transportation service, to service and repair aircraft and generally deal in all kinds of airplanes, seaplanes, oil, fuel, aircraft accessories and equipment and goods, wares and merchandise necessary for its transportation service, and to purchase, rent or otherwise acquire, to hold, own,

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mortgage, pledge, assign, transfer, lease or otherwise encumber or dispose of any property, right or interest which may be in any way connected with or useful to the business conducted by the Corporation, to borrow and lend money in aid of the Company's corporate purposes, and for such purposes, to issue, receive and hold bonds, notes and other obligations; to appoint subject at all times to the supervision and control of the Board of Directors, a manager or managers, to attend to the proper conduct of the business of the corporation, and further to engage in all other acts and business which may be necessary or convenient in the furtherance of the air transportation business, including but not limited to the management of operations of, or investment in hotels, restaurants, cafes and amusement enterprises of all kinds and generally dealing in and with all facilities and appurtenances desirable or appropriate in the conduct of the foregoing activities".

PAL is the registered owner of six (6) parcels of land without any improvements constructed thereon, all located in Barangay Yapak, Municipality of Malay, Province of Aklan, (hereinafter referred to as the "Subject Properties") which are specifically described, as follows:

Transfer Certificate of Title Nos.	Tax Declaration Nos.	Area (in Sqm.)	Classification
[redacted]	[redacted]	17,470	Agricultural
[redacted]	[redacted]	1,412	Residential
[redacted]	[redacted]	115,611	Agricultural
[redacted]	[redacted]	6,238	Agricultural
[redacted]	[redacted]	5,166	Agricultural
[redacted]	[redacted]	23,312	Agricultural

The Subject Properties were lodged under "Non-current Assets" caption of PAL's Audited Financial Statement with the account title "Investment Properties". The Subject Properties remain idle and undeveloped and were never used in trade or business by PAL.

On August 25, 2020, a Contract to Sell was executed between PAL, as the Vendor, and Golden TW Realty & Development Corporation, as the Vendee, whereby the latter offered to purchase from the Vendor the Subject Properties on an "as is where is basis", and the Vendor accepted such offer to purchase.

The issue is whether or not the Subject Properties are capital assets of PAL.

In reply, please be informed that the term "capital asset" as negatively defined in Section 39(A)(1) of the National Internal Revenue Code (Tax Code) of 1997, as amended, 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 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.

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An idle property may be classified as capital asset or ordinary asset. Revenue Regulations (RR) No. 7-2003, particularly Section 3(e) thereof, provides to wit:

> **"SEC. 3. GUIDELINES IN DETERMINING WHETHER A PARTICULAR REAL PROPERTY IS A CAPITAL ASSET OR ORDINARY ASSET. –**
>
> xxx xxx xxx
>
> e. Treatment of abandoned and idle real properties. – Real properties formerly forming part of the stock in trade of a taxpayer engaged in the real estate business, or formerly being used in the trade or business of a taxpayer engaged or not engaged in the real estate business, which were later on abandoned and became idle, shall continue to be treated as ordinary assets. Real property initially acquired by a taxpayer engaged in the real estate business shall not result in its conversion into a capital asset even if the same is subsequently abandoned or becomes idle.
>
> Provided however, that *properties classified as ordinary assets for being used in business by a taxpayer engaged in business other than real estate business as defined in Section 2(g) hereof are automatically converted into capital assets upon showing of proof that the same have not been used in business for more than two (2) years prior to the consummation of the taxable transactions involving said properties*. (Emphasis supplied)

Based on the above, an idle property classified as ordinary asset is automatically converted into capital asset upon showing of proof that the same has not been used in business for more than two (2) years prior to the consummation of the taxable transaction involving said properties. The automatic conversion of property into capital asset provided in RR No. 7-2003, however, is not necessary when the idle real property is considered capital asset from the moment it was acquired. The Subject Properties were registered in the name of PAL in 2017 and were acquired for investment purposes and recorded by PAL as capital assets. The properties were never used in the course of trade or business of PAL, or depreciated for that purposes. No improvements were introduced to the Subject Properties as certified by the Provincial Assessor's Office of the Province of Aklan and Barangay Chairman of Barangay Yapak, Municipality of Malay, Province of Aklan. More importantly, PAL is engaged in air transportation of passengers and cargoes and not in the real estate business.

In view of the foregoing, and considering that PAL is a taxpayer not engaged in the real estate business, being not a real estate dealer, developer or lessor and was organized as an airline company; that the Subject Properties have been idle and vacant (for more than two years) as shown, aside from the pictures submitted, by the Certifications of the Provincial Assessor's Office of the Province of Aklan and Barangay Chairman of Barangay Yapak, Municipality of Malay, Province of Aklan that there are no improvements nor structures erected on the Subject Properties; and that the Subject Properties have been treated in the books of accounts and are reflected in the audited

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financial statement as investment properties and have not been used in the ordinary course of trade or business, it is the considered opinion of this Office that the Subject Properties described above are classified as capital assets, the conveyance of which is subject only to the CGT under Section 27(D)(5) of the Tax Code and DST under Section 196 of the same Code, and shall not be subject to VAT under Section 106 of the same Code *(BIR Ruling Nos. 187-2017 dated April 17, 2017; 634-2017 dated December 19, 2017 and 480-2017 dated October 18, 2017; VAT-0404-2020 dated July 23, 2020)*

This ruling is being issued on the basis of the foregoing facts as represented. However, if upon investigation, it will be disclosed 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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gps (PAL)