REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

EXQUISITE PAWNSHOP AND JEWELRY, INC.,
Petitioner,

- versus -

C.T.A. CASE NO. 5741

CRISPINO VALLEJOS, JR., in his capacity as Revenue Regional Director, Revenue Region No. 13; and COMMISSIONER OF INTERNAL REVENUE,
Respondents.

Promulgated:
APR 24 2000

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DECISION

The decision of Respondent Revenue Regional Director Crispino Vallejos, Jr. denying Petitioner's protest on the assessment of the 5% lending investor's tax is being assailed in this Petition for Review on questions of law.

The antecedent facts follow.

Petitioner is a domestic corporation organized and existing under the laws of the Republic of the Philippines, and is the owner and operator of Exquisite Pawnshop and Jewelry, Inc. located at A. Del Rosario Street, Mandaue City.

On March 11, 1991 and May 27, 1991, the then Commissioner of Internal Revenue Jose U. Ong issued Revenue Memorandum Order (RMO) No. 15-91 and Revenue Memorandum Circular (RMC) No. 43-91 subjecting all pawnshops to a five (5%) percent lending investor's tax applying Section 116 of the Tax Code (Annexes B and C, Petition for Review), which provides, thus:

> "**Section 116. Percentage tax on dealers in securities, lending investors.** - x x x Lending investors shall pay a tax equivalent to five (5%) per cent of their gross income."

Pursuant to the said RMO 15-91 and RMC 43-91, Respondent Revenue Regional Director for Revenue Region No. 13, through its Assessment Division, issued to Petitioner a Pre-Assessment Notice dated April 2, 1998, with an attached Computation of Business' Tax Deficiency for the year 1995 representing the five (5%) percent lending investors' tax (Annexes D and D-1, Petition for Review).

On May 25, 1998, Petitioner received Assessment Notice No. 80-PT-13-96-98-5-0, together with a letter showing the details of the assessment dated April 20, 1998, demanding payment of the sum of P649,255.49, inclusive of interest and surcharge (Annexes E and E-1, Petition for Review). Petitioner then filed a formal protest on June 17, 1998 contesting said assessment, thus:

x x x x x x x x x

> "Your letter mentions about a Court of Appeals case. Please take administrative notice that the case you are referring to is entitled and docketed as "Commissioner of Internal Revenue vs. Honorable Andres B. Reyes, Jr., et. al., CA GR Sp. No. 28824", Court of Appeals Metro Manila. It is correct to state that in such Decision of the Court of Appeals ruled that a Pawnshop is not a Lending Investor and a Pawn Ticket is not liable to pay documentary stamp tax. On the basis of such ruling, RMO No. 15-91 and RMC No. 43-91 providing liabilities for payment of these taxes were considered null and void.
>
> This Formal Tax Protest is made therefore on the basis of the arguments submitted by the aggrieved taxpayer in that case as well as the findings of facts and law cited in such Decision. Our client adopts substantially all arguments presented thereat, to wit:
>
> 1. Lending Investor specified and defined under the tax code is not a pawnshop. Neither is a Pawnshop defined to include a Lending Investor. This fact is clearly established in Section 192 of the National

Internal Revenue Code, as amended by Presidential Decree No. 1739 where a Lending Investor is treated separately from Pawnshop in the assessment of "Other Fixed Taxes".

It is undisputed that Pawnshops are not mentioned under Section 209 of the NIRC, as amended by President (sic) Decree No. 1739, when said proviso imposed Percentage Taxes on Dealers in Securities and Lending Investors. Not being mentioned, Pawnshops are therefore not subject to percentage taxes now sought to be collected in the aforecited Assessment Notice and Demand.

The reason that Pawnshop is treated differently from a Lending Investor certainly lies on the fact that Pawnshop Operations are refulated, monitored and supervised strictly by the Central Bank pursuant to Pawnshop Regulatory Act which is Presidential Decree No. 114. What surely prompted the law to hold a tight protective grip on the lending public from pawnshop operations could be the fact that mostly only small borrowers are the clients of these pawnshops. Conversely, there is no law applicable at the moment governing Lending Investors. Lending Investors' rates of interests are not fixed or pegged by the Central Bank and their transactions enjoy so much freedom and flexibility.

2. The Internal Revenue Commission has no authority to create and impose whatever taxes. Only the Legislative Branch of the Government is empowered to do so. If the Commission does so, it usurps an authority which belongs to another instrumentality of the government.

BIR Circulars are supposed to be issued to implement and enforce – and these ONLY – tax laws duly mandated by Congress. Unfortunately, Revenue Circulars Nos. 15-91 and 43-91 no longer simply enforce or implement a tax law. These questioned Circulars actually have illegally created a New and/or Additional Tax Law imposing tax liabilities on Pawnshops.

3. That decision in the case of "Commissioner of Internal Revenue vs. Honorable Reyes", supra, being a Decision rendered by the Court of Appeals – a collegiate or superior court – partakes of the nature of a law of the land. Thus, said decision, unless reversed by the Supreme Court, has the effect of nullifying the questioned Revenue Memorandum Circulars under which the Bureau is imposing the tax."

Respondent Revenue Regional Director, in a letter dated February 3, 1999 and received by the Petitioner on February 10, 1999, denied the protest and upheld the propriety of the assessment of the 5% lending investors' tax by stating that in BIR Ruling No. 221-91 dated October 30, 1991, the definition of the term "Lending Investor" under Section 194(u) [should be Section 157(u)] includes "all persons who make a practice of lending money for themselves or others at interest", hence, encompasses the activity of a pawnshop operator (Annex A, Petition for Review).

On March 12, 1999, the instant petition was filed by Petitioner and raised the following arguments:

1.) There is no specific provision in either the Tax Code or the VAT law which expressly imposes on pawnshops the 5% tax on its gross income.

2.) Pawnshops are widely different from lending Investors which are subject to the 5% tax on gross income under the specific provisions of law.

3.) The law is clear that a pawn ticket is not subject to documentary stamp tax.

4.) RMO No. 15-91 and RMC No. 43-91 are null and void, for the following reasons:

a) RMO No. 15-91 and RMC No. 43-91 are not enforcing any particular provision of the internal revenue laws, but is legislating a new and additional tax measure on pawnshops.

b) The Commissioner of Internal Revenue (CIR), in the guise of regulation through the issuance of RMO No. 15-91 and RMC No. 43-91, has usurped the power conferred only upon Congress, thereby making said issuances null and void.

5.) The enforcement/implementation of RMO No. 15-91 and RMC No. 43-91, must be held in abeyance pending the decision of the Supreme Court in CIR vs. Court of Appeals, et al, G.R. No. 113459.

On the other hand, Respondent claimed, by way of Special and Affirmative Defenses, that:

x x x x x x x x x

"7.) Under the Tax Code, the Commissioner of Internal Revenue is empowered "to make rulings or opinions in connection with the implementation of the provisions of internal revenue laws", thus:

> "SEC. 245. Authority of the Secretary of Finance to promulgate rules and regulations. - The Secretary of Finance, upon recommendation of the Commissioner, shall promulgate all needful rules and regulations for the effective enforcement of the provisions of this Code.
>
> "The authority of the Secretary of Finance to determine articles similar or analogous to those subject to a rate of sales tax under certain category enumerated in sections 163 and 165 of this Code shall be without prejudice to the <u>power of the Commissioner of Internal Revenue to make rulings or opinions in connection with the implementation of the provisions of internal revenue laws,</u> including rulings on the classification of articles for sales and similar purposes." (Underscoring ours)

8.) Previous BIR rulings that pawnshops are not subject to the 5% lending investor's tax and that a pawn ticket is not subject to documentary stamp tax, are rules interpreting the provisions of the Tax Code. RMO 15-91 and RMC 43-91 which expressly revoked said rulings are rules interpreting the very same provisions of the Tax Code. They are not new and additional tax measures but new rulings or opinions. The revocation of rulings is authorized under section 246 of the Tax Code, thus:

> SEC. 246. <u>Non-retroactivity of rulings.</u> - "Any revocation, modification or reversal of any of the rules and regulations promulgated in accordance with the preceding section or any of the rulings or circulars promulgated by the Commissioner shall not be given retroactive application x x x."

9.) It has been held that the incumbent is not bound by the previous ruling of his predecessor if he is satisfied that a different construction of the statute should be given [Hilado v. Collector of Internal Revenue, 100 Phil. 288, 294 (1956)].

10.) The legal definition of "lending investor" is broad enough to cover pawnshop operators. As defined by law, "lending investor" includes all persons who make a practice of lending money for themselves or others at interest [Sec. 157(u), Tax Code]. On the other hand, Section 3 of Presidential Decree No. 114 defines a "pawnshop", thus:

> "Pawnshop" shall refer to a person or entity engaged in the business of lending money on personal property delivered as security for loans and shall be synonymous, and may be used interchangeably, with pawn broker or pawnbrokerage." (Underscoring ours)

Since the principal business activity of a pawnshop is lending money at interest, it easily falls under the definition of "lending investor". From the definition of "lending investor", the liability of pawnshops to the 5% lending investor's tax is explicit.

11.) Pawnshops lend money on the security of personal property, that is, a pledge. The pledge is evidenced by a pawn ticket. hence, the pawn ticket is the logical document subject to the documentary stamp tax on pledges under Section 195 of the Tax Code which provides:

> "SEC. 195. Stamp tax on mortgages, pledges, and deeds of trust. - On every mortgage or pledge of lands, estate, or property, real or personal, heritable or movable, whatsoever, where the same shall be made as a security for the payment of any definite and certain sum of money lent at the time or previously due and owing or forborne to be paid being payable, and on any conveyance of land, estate, or property whatsoever, in trust or to be sold, or otherwise converted into money there shall be collected a documentary stamp tax with the following rates; x x x". (Underscoring ours)

12.) The assessment in question was issued in accordance with law and pertinent regulations.

13.) All presumptions are in favor of the correctness of tax assessments (CIR vs. Construction Resources of Asia, Inc., 145 SCRA 671) and the burden of proof to prove otherwise is upon petitioner."

The issues We are tasked to resolve have been limited and agreed upon by the parties to be as follows:

(1) Whether or not pawnshops, under the Tax Code, are covered by the percentage tax imposed against lending investors; and

(2) Whether or not RMO No. 15-91 and RMC No. 43-91, pursuant to which the assessment and collection of the five (5%) percent lending investors' tax on pawnshops are made, are valid and enforceable.

For purposes of clarity, the pertinent provisions of the laws involved are hereunder quoted:

A. Title V, Chapter I on Definitions of the Tax Code, as amended (1986)

Section 157. Words and phrases defined. - x-x-x

(u) *"Lending investor" includes <u>all persons who make a practice of lending money</u> for themselves or others <u>at interest</u>.*

B. Title V, Chapter II on Tax on Business of the Tax Code, as amended (1986)

Section 161. Fixed taxes. - x-x-x

(3) Other fixed taxes. - x-x-x

<u>(dd) Lending Investors</u> -

1. In chartered cities and first class municipalities, one thousand pesos.

2. In second and third class municipalities, five hundred pesos;

*3. In fourth and fifth class municipalities and municipal districts, two hundred fifty pesos: **Provided**, That lending investors who do business as such in more than one province shall pay a tax of one thousand pesos.*

x-x-x x-x-x x-x-x

<u>(ff) Pawnshops</u>, *one thousand pesos.*

x-x-x x-x-x x-x-x

Section 175. Percentage tax on dealers in securities, lending investors. - *Dealers in securities shall pay a tax equivalent to six (6%) per cent of their gross income. Lending investors shall pay a tax equivalent to five (5%) per cent of their gross income. (As amended by PD 1739, PD 1959 and PD 1994)*

C. Presidential Decree No. 114, otherwise known as the Pawnshop Regulation Act

Sec. 3. *Definitions.* - As used in this Decree, unless the context otherwise requires, the following terms shall have the following meanings:

"Pawnshop" shall refer to a person or entity engaged in the business of lending money on personal property delivered as security for loans and shall be synonymous, and may be used interchangeably, with pawnbroker **or** pawnbrokerage.

x-x-x x-x-x x-x-x

Sec. 10. *Rates of interest.* -No pawnshop shall directly or indirectly stipulate, charge, demand, take or receive any higher rate or greater sum or value for any loan or forbearance than the rate allowed by the Usury Law for such transactions. x-x-x

(Emphasis and underscoring supplied)

At the outset, the argument of the Respondent that pawnshops are lending investors pursuant to the latter's definition under then Section 157(u) of the Tax Code, as amended, *supra*, would seem to hold water in the light of the fact that a pawnshop is undeniably in the habit of lending money at interest. This can be discerned readily from the provisions of the Pawnshop Regulation Act (P.D. 114) which under Sections 3 and 10 thereof, *supra*, describes a pawnshop as "a person or entity engaged in the business of lending money" with none of it directly or indirectly stipulating, charging, demanding, taking or receiving "any higher rate or greater sum or value for any loan or forbearance than the rate allowed by the Usury Law for such transactions."

Relying on his authority under Sections 245 and 246 of the Tax Code, as amended, to make rulings or opinions in connection with the implementation of the provisions thereof and to revoke, modify or reverse the same, Respondent officially revoked BIR rulings exempting pawnshops from the 5 % lending investors' tax by issuing the now disputed RMC 15-91and RMO 43-91.

After a more careful scrutiny of the legal and factual milieu of the case at bar, more particularly on the underlying reasons behind the decision of the Court of Appeals case cited in Petitioner's protest letter hereinbefore quoted, We are constrained to disagree from the viewpoint adopted by the Respondent. By clear legislative intent, We find pawnshops not subject to the 5% lending investors' tax provided under Section 116 of the Tax Code, as amended.

We are in a situation where to adopt the literal import of the provisions of Section 157(u) in relation to Section 116 of the Tax Code, as amended, would lead to plain absurdity, injustice, contradiction and impairment of Constitutional limitations. For this reason, We are interpreting said provisions according to the principle of *ratio legis* or spirit or reason of the law. Thus:

> The principle has been variously formulated: "As a general rule of statutory construction, the spirit or intention of a statute prevails over the letter thereof, and what is within the spirit of a statute is within the statute although it is not within the letter thereof, while that which is within the letter but not within the spirit of the statute is not within the statute." **[Tanada vs. Cuenco, 103 Phil. 1051, 1086 (1957), citing 82 C.J.S. 613]** The spirit, rather than the letter, of a statute determines the construction thereof, and the court looks less to its words and more to its context, subject matter, consequence and effect. **[Manila Race Horse Trainers Assn., Inc. vs. De la Fuente, 88 Phil. 60 (1951); Go Chi vs. Go Cho, 96 Phil. 622 (1955)]** A statute must be read according to its spirit and intent, and where the legislative intent apparently conflicts with the letter of the law, the former prevails over the latter. **[Tanada vs. Cuenco, 103 Phil. 1051 (1957); Hidalgo vs. Hidalgo, G.R. No. 25326, May 29, 1970, 33 SCRA 105 (1970); Roa vs. Commissioner of Customs, 23 Phil. 315 (1912)]**

(All citations taken from the book: Statutory Construction by Agpalo, 3rd ed., 1995)

If We go by the contention that pawnshops are lending investors, then Congress would not have been mistaken in treating the two separately under paragraphs (*dd*) and (*ff*) of Section 161 of the Tax Code, as amended, *supra*. Logic simply dictates that if by prior definition under Section 157 (u) of said Code pawnshops and lending investors are of the same class, then there is no rational basis for differentiating them under one heading later, except for the fact that they are dissimilar as tax subjects.

Further analyzing said Section 161, it appears that lending investors were imposed a graduated type of fixed taxes depending on the class of the city or municipality involved while pawnshops were differently levied a flat rate of tax. This particular observation bolsters Our position that pawnshops are not similarly situated as lending investors. Congress would not have intended otherwise because the act of segregating and imposing upon them unequal amount of taxes would transgress the fundamental rule on taxation on uniformity or equality enshrined under par. 1, Section 28 of Article VI of our Constitution. The rule requires that all subjects or objects of taxation, similarly situated, are to be treated alike or put on equal footing both in privileges and liabilities **(Juan Luna Subdivision vs. Sarmiento, 91 Phil. 371)** It has also been interpreted to mean that all taxable articles or kinds of property of the same class shall be taxed at the same rate **(City of Baguio vs. de Leon, 25 SCRA 938)**. Verily, Congress is presumed to have acted in full knowledge of this particular constitutional limitation when it classified pawnshops apart from lending investors.

In the same vein, We take note of the fact that there are additional provisions of the Tax Code, as amended, which treats of other persons or entities also engaged in the practice of lending money at interest differently from a lending investor. We are referring to banks, non-bank financial intermediaries and finance companies who are in the lending business earning interest too, yet, are classified separately and imposed a graduated type of rate of taxes (5%, 3%, 1% & 0%) under Sections 119 and 120 of said Code.

Again, if We go by definition and the rule on uniformity, banks, non-bank financial intermediaries and finance companies are supposed to be simply imposed a tax rate of 5% on their gross income because they do meet the criteria of what a lending investor should be. The fact shows, however, that they are treated differently.

Moreover, both Sections 119 and 120 of the Tax Code, as amended, carry a proviso granting the Commissioner of BIR the right to impose the same taxes on persons performing similar banking or financing activities, as the case may be, while Section 116 of the same Code governing lending investors has none of the same. If the legislature intended to include other persons or entities engaged in similar lending activities, such as pawnshops, under the term "lending investors", it would have conveniently added the same proviso. In the absence of such proviso, it would seem thus that lending investors are persons or entities of their own class, without any need for the Commissioner to classify other persons or entities engaged in similar lending activities.

What We have presented so far in the preceding discussion succinctly demonstrates the erroneous decision reached by Respondent Commissioner in classifying pawnshops as lending investors subject to the 5% lending investors' tax. Inevitably, We reach the conclusion that the term "lending investor" as defined in Section 157(u) should be taken in isolation and should serve no other purpose than to simply clarify what a "lending investor" is all about. Indeed, as pointed out by the Petitioner, there is no special law governing lending investors (p.8, Petition for Review). Without any legal or dictionary meaning of what a lending investor is, this lexicological vacuum could have very well been the sole justification for the existence of said definition.

And even if We assume for the sake of argument that the stance of Respondent Commissioner has some support in fact and in law, Our pronouncements herein would still leave so much doubt when the same is put to the crucible of judicial scrutiny. In this light, the correct interpretation should still be in favor of the Petitioner. As was held in the case of **Commissioner of Internal Revenue vs. Fireman's Fund Insurance Company, 148 SCRA 315**, citing the case of **Manila Railroad Co. v. Collector of Customs, 52 Phil. 950 [1929])**, to wit:

> "It is a general rule in the interpretation of statutes levying taxes or duties, that in case of doubt, such statutes are to be construed most strongly against the government and in favor of the subjects or citizens, because burdens are not to be imposed, nor presumed to be imposed beyond what statutes expressly and clearly import."

With reference to the second issue, We rule in the negative. As correctly pointed out by Petitioner in its memorandum, the issuance of RMO 15-91 and RMC 43-91 is a usurpation of the prerogative, power and authority of Congress (p. 96, CTA Records). In fact, the Court of Appeals, in the aforecited **case of Commissioner of Internal Revenue vs. Hon. Andres Reyes, C.A.-GR Sp. No. 28824,** ruled impugning the validity of the said revenue regulations, thus:

> "x x x. Revenue Circulars Nos. 15-91 and 43-91 are not implementing rules but are new and additional measures which only congress is empowered to impose. Section 245 of the Tax Code has limited or confined petitioner's power to issuing rules and regulation to implement or carry into effect the provision of the Code in the enforcement of taxes provided therein, and petitioner cannot impose additional taxes not provided therein.
>
> Under the Constitution, the power to tax is solely vested in Congress. In issuing subject Revenue Circulars imposing new taxes against pawnshop, petitioner arrogated unto himself legislative powers, with grave abuse of discretion and in excess of jurisdiction."

Finally, We resolve not to dwell into the merits of the imposition of documentary stamp tax on pledges contracted by pawnshops in view of the fact that it does not form part of the assessment in question. This loophole prevents Petitioner from making a protest over it, much more appeal the same before this Court.

WHEREFORE, in view of the foregoing, the instant Petition for Review is hereby **GRANTED**. Revenue Memorandum Circular No. 43-91 and Revenue Memorandum Order No. 15-91, in so far as they classify pawnshops as lending investors subject to the 5% lending investors' tax under Section 116 of the Tax Code, as amended, are hereby declared **NULL AND VOID**. **ACCORDINGLY**, Assessment Notice No. 80-PT-13-96-98-5-0, dated April 20, 1998 is hereby declared **CANCELLED, WITHDRAWN and WITH NO FORCE AND EFFECT**.

SO ORDERED.

RAMON O. DE VEYRA
Associate Judge

WE CONCUR:

ERNESTO D. ACOSTA
Presiding Judge

AMANCIO Q. SAGA
Associate Judge

CERTIFICATION

I hereby certify that the above decision was reached after due consultation with the members of the Court of Tax Appeals in accordance with Section 13, Article VIII of the Constitution.

ERNESTO D. ACOSTA
Presiding Judge