REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

SECOND DIVISION

CENTURY PEAK PROPERTY DEVELOPMENT, INC. and KINGSVILLE INTERNATIONAL RESOURCES, INC.,
Petitioners,

- versus –

THE SECRETARY OF FINANCE and COMMISSIONER OF INTERNAL REVENUE,
Respondents.

CTA Case No. 9145

Members:

CASTAÑEDA, JR., *Chairperson,*
CASANOVA, and
MANAHAN, *JJ.*

Promulgated:

JUL 2 4 2017
11:10 a.m.

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DECISION

CASTAÑEDA, JR., *J.:*

THE CASE

This is a Petition for Review[1] filed by Century Peak Property Development, Inc. and Kingsville International Resources, Inc., praying for the reversal of Certification Ruling SN. 014-2012 and Department of Finance (DOF) Resolution dated July 14, 2015 and the

[1] Docket vol. I, pp. 10-29.

declaration that no value-added tax (VAT) is imposable on the Deed of Assignment executed by petitioners on October 13, 2010.

THE FACTS

Petitioner Century Peak Property Development, Inc.[2] ("Century Peak" for brevity) is a domestic corporation duly organized and existing in accordance with the laws of the Republic of the Philippines, with Tax Identification No. 007-933-304. Its principal office address is at 902 Imperial Bayfront Tower, 1642 A. Mabini Street, Malate, Manila, Philippines.[3]

Petitioner Kingsville International Resources, Inc. ("Kingsville" for brevity) is a corporation duly organized under the laws of the Republic of the Philippines, with Tax Identification No. 000-780-199-000. Its principal office address is at 2nd Floor Harrison Shoe Plaza, 3030 Agtarap Street corner F.B. Harrison Street, Pasay City, Metro Manila, Philippines.[4]

Respondent Secretary of Finance (SOF) is the head of the Department of Finance, a department of government, with principal office address at DOF Building, Bangko Sentral Complex, Roxas Boulevard, 1004 Manila.[5]

Respondent Commissioner of Internal Revenue (CIR) is the chief of the Bureau of Internal Revenue (BIR), an instrumentality of government, with main address at the BIR National Office Building, BIR Road, Diliman, Quezon City.[6]

Petitioner Kingsville is the registered owner of two (2) parcels of land covered by Transfer Certificate of Title No. 180739[7] and Transfer Certificate of Title No. 180740[8] located at Lots 2 and 3, Block 359, *jc*

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[2] Currently named as "Century Peak Hotel Management and Development, Inc."
[3] Par. 1, Parties, Facts Stipulated, Joint Stipulation of Facts and Issues (JSFI), docket vol. II, p. 537; Exhibits "P-2", "P-3", "P-4", "P-5", "P-6", and "P-7", docket vol. II, pp. 565-597.
[4] Par. 2, Parties, Facts Stipulated, JSFI, docket vol. II, p. 538; Exhibits "P-8" and "P-9", docket vol. II, pp. 598-610.
[5] Par. 3, Parties, Facts Stipulated, JSFI, docket vol. II, p. 538.
[6] Par. 4, Parties, Facts Stipulated, JSFI, docket vol. II, p. 538.
[7] Exhibit "P-12", docket vol. II, pp. 621-625.
[8] Exhibit "P-13", docket vol. II, pp. 626-630.

corner Sta. Monica and Adriatico Streets, Zone 72, Barangay 668, Malate, Manila.[9]

On October 13, 2010, petitioner Kingsville executed a Deed of Assignment[10] involving the two parcels of land covered by Transfer Certificate of Title No. 180739 and Transfer Certificate of Title No. 180740 for and in consideration of petitioner Kingsville's total subscription of 450,000 shares at ₱100 per share in the capital stock of petitioner Century Peak.[11]

On December 21, 2010, the Securities and Exchange Commission (SEC) issued the Certificate of Incorporation of petitioner Century Peak.[12]

On May 16, 2011, petitioner Century Peak filed its Request for BIR Confirmation Ruling[13] before respondent CIR.[14]

On October 18, 2011, petitioner Century Peak filed before respondent CIR its Compliance Letter[15] submitting before respondent CIR the additional information in support of the Request for BIR Confirmation Ruling.[16]

Acting on the request, respondent CIR issued Certification Ruling SN. 014-2012[17] dated February 20, 2012 and certified that on the basis of the representations and documents submitted, the transfer of the properties by and between Kingsville International Resources Inc. and Century Peak Development Inc. is not subject to income tax, capital gains tax, expanded withholding tax, and donor's tax. However, the transaction is subject to documentary stamp tax and value-added tax at twelve percent (12%) in the amount of ₱5,416,164.00.[18]

[9] Par. 7, Surrounding Circumstances, Facts Stipulated, JSFI, docket vol. II, p. 538.
[10] Exhibit "P-14", docket vol. II, pp. 631-634.
[11] Par. 8, Surrounding Circumstances, Facts Stipulated, JSFI, docket vol. II, pp. 538-539.
[12] Par. 9, Surrounding Circumstances, Facts Stipulated, JSFI, docket vol. II, p. 539.
[13] Exhibit "P-16" docket vol. II, pp. 493-495.
[14] Par. 10, Surrounding Circumstances, Facts Stipulated, JSFI, docket vol. II, p. 539.
[15] Exhibit "P-17", docket vol. II, pp. 496-500.
[16] Par. 11, Surrounding Circumstances, Facts Stipulated, JSFI, docket vol. II, p. 539.
[17] Exhibit "P-11", docket vol. II, pp. 615-620.
[18] Par. 12, Surrounding Circumstances, Facts Stipulated, JSFI, docket vol. II, p. 539.

Thereafter, petitioner Century Peak filed with respondent CIR its Request for Reconsideration and Revision of Certification Ruling SN. 014-2012[19] on March 9, 2012.[20]

In response thereto, respondent CIR sent to petitioner Century Peak the Letter[21] dated April 16, 2012 with Reference No. M-039-2012, stating that the request for reconsideration should be filed with the Secretary of Finance in accordance with Section 3 of DOF Order No. 007-02 dated May 7, 2002.[22]

Petitioner Century Peak filed before the office of respondent SOF its Request for Revision[23] dated May 24, 2012, which was treated as a request for review of BIR Certification Ruling SN. 014-2012.[24]

Respondent SOF acted on the request for review of petitioner Century Peak and issued the assailed Resolution[25] dated July 14, 2015.[26]

On September 11, 2015, petitioners filed the instant Petition for Review[27].

Within the extended time granted by the Court,[28] respondent CIR filed his Answer[29] on November 23, 2015 interposing the following special and affirmative defenses:

"SPECIAL AND AFFIRMATIVE DEFENSES

4. Respondent reiterates and re-pleads the preceding paragraphs of this Answer as part of her Special and Affirmative Defense.

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[19] Exhibit "P-18", docket vol. II, pp. 501-503.
[20] Par. 13, Surrounding Circumstances, Facts Stipulated, JSFI, docket vol. II, p. 539.
[21] Exhibit "P-19", docket vol. II, pp. 504-505.
[22] Par. 14, Surrounding Circumstances, Facts Stipulated, JSFI, docket vol. II, p. 539.
[23] Exhibit "P-20", docket vol. II, pp. 506-513.
[24] Par. 15, Surrounding Circumstances, Facts Stipulated, JSFI, docket vol. II, p. 539.
[25] Exhibit "P-10", docket vol. II, pp. 611-614.
[26] Par. 16, Surrounding Circumstances, Facts Stipulated, JSFI, docket vol. II, p. 539.
[27] Docket vol. I, pp. 10-29.
[28] Orders dated October 6, 2015 and November 3, 2015, docket vol. I, pp. 137 and 151.
[29] Docket vol. I, pp. 159-166.

The transfer of the two (2) parcels of land by Kingsville International Resources, Inc. (Kingsville) to Century Peak Property Development, Inc. (Century) is a considered as a 'sale, barter or exchange of goods' subject to Value Added Tax (VAT).

5. Petitioners maintained that the transfer of the two (2) parcels of land from Kingsville to Century is not subject to VAT since it cannot be considered as a 'sale, barter or exchange of goods'.

6. Respondent differs.

7. The transfer of the two (2) parcels of land is a transaction subject to VAT.

8. First, Kingsville is a corporation primarily engaged in the sale of real estate. In fact, the parcels of land were goods it held primarily for sale.

9. Section 106 of the National Internal Revenue Code (Tax Code) states:

> **SEC. 106. Value-Added Tax on Sale of Goods or Properties.** –
>
> (A) Rate and Base of Tax. – **There shall be levied, assessed and collected on every sale, barter or exchange of goods or properties**, value-added tax equivalent to [twelve percent (12%)] of the gross selling price or gross value in money of the goods or properties sold, bartered or exchanged, such tax to be paid by the seller or transferor.
>
> (1) **The term 'goods' or 'properties'** shall mean all tangible and intangible objects

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which are capable of pecuniary estimation and **shall include**:

(a) Real properties held primarily for sale to customers or held for lease in the ordinary course of trade or business;

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(**Emphasis supplied**).

10. More importantly, the alleged Deed of Assignment is clear, there was an exchange of property between Kingsville and Century. It states:

For and inconsideration of the full payment of KINGSVILLE's total subscription of Four Hundred Fifty Thousand (450,000) shares at One Hundred Pesos (P100.00) per share in capital stock of CENTURY PEAK PROPERTY DEVELOPMENT INC., a corporation that is not in the process of incorporation under the laws of the Republic of the Philippines, **KINGSVILLE hereby assigns, transfers and conveys unto CENTURY PEAK PROPERTY DEVELOPMENT, INC. all its rights titles and ownership** over the following properties consisting of:

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With the assignment and transfer of all rights, title and ownership of KINGSVILLE over the above-described parcels of land unto CENTURY PEAK PROPERTY DEVELOPMENT INC., the latter shall assume all obligations over the above described parcels of land in favor of KINGSVILLE as assignor.

(**Emphasis supplied**).

11. Clearly, there transfer was an exchange of property between Kingsville and Century; that is the two (2) parcels of land in exchange for four hundred fifty thousand (450,000) shares.

12. Thus, there being a transfer of absolute ownership of the parcels of land held primarily for sale from Kingsville to Century, the transaction is subject to VAT pursuant to clear provisions of the Tax Code.

Revenue Regulations No. 4-2007 is inapplicable.

13. Petitioner argued that Revenue Regulations No. 4-2007 (RR 4-07) is applicable since at it was the prevailing regulation at the time of the execution of the alleged Deed of Assignment.

14. Respondent disagrees.

15. Section 4-106-8 of RR 4-07 states:

> **Section 8. CHANGE OR CESSATION OF STATUS AS VAT REGISTERED PERSON.** - Sec. 4.106-8 of RR No. 16-2005 is hereby amended to read as follows:
>
> SEC. 4.106-8. Change or Cessation of Status as VAT-registered Person.
>
> -xxx-
>
> **(b) Not subject to output tax**
>
> The VAT shall not apply to goods or properties existing as of the occurrence of the following:
>
> **(1) Change of control of a corporation by the acquisition of the controlling interest of such corporation by**

> **another stockholder or group of stockholders**. The goods or properties used in business or those comprising the stock-in-trade of the corporation, having a change in corporate control, will not be considered sold, bartered or exchanged despite the change in the ownership interest in the said corporation.
>
> Illustration: Abel Corporation is a merchandising concern and has an inventory of goods for sale amounting to Php 1 million. Nel Corporation, a real estate developer, exchanged its real estate properties for the shares of stocks of Abel Corporation resulting to the acquisition of corporate control. The inventory of goods owned by Abel Corporation (Php 1 million worth) is not subject to output tax despite the change in corporate control because the same corporation still owns them. This is in recognition of the separate and distinct personality of the corporation from its stockholders. However, the exchange of real estate properties held for sale or for lease, for shares of stocks, whether resulting to corporate control or not, is subject to VAT, subject to exceptions provided under Section 4.106-3 hereof. **On the other hand, if the transferee of the transferred real property by a real estate dealer is another real estate dealer, in an exchange where the transferor gains control of the transferee-corporation, no output VAT is imposable on the said transfer.**

16. In the first place, there was no change of control of a corporation to speak of. As admitted by petitioners, at the time of the taxable event, there was no Century to speak of. Thus, there was nothing to gain control of. *yz*

17. Second, the provision being invoked by petitioner clearly intended that there be two (2) corporations already in existence. The requirement that the transferee and the transferor need to be a real estate dealer bolsters this argument.

18. It is elementary that a corporation only gains its juridical personality upon the approval of its corporate papers by the Securities and Exchange Commission (SEC).

19. As here, Century was yet to be formed. Thus, at the time of the taxable event there was no other corporation to speak of.

20. Even assuming but definitely no conceding that Century is already in existence since it was in the process of incorporating, it was yet to be determined that it will engage in real estate business.

21. Thus, the requirements of Section 4-106-8 of RR 4-07 that there be a (1) corporation and (2) engaged in real estate business was never satisfied and thus, it Section 4-106-8 of RR 4-07 finds no applicability whatsoever in the instant case."

Upon motion,[30] respondent SOF, in an Order[31] dated November 6, 2015, was given a non-extendible period of fifteen (15) days from October 30, 2015 or until November 14, 2015 within which to file his Answer.

On November 16, 2015, respondent SOF filed through registered mail a Motion for Reconsideration of the Order dated 6 November 2015 with Motion for Additional Period of Time to File Responsive Pleading[32]. Thereafter, on December 1, 2015, respondent SOF filed through registered mail a Motion to Admit Answer.

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[30] Motion for Further Extension of Time to File Responsive Pleading, docket vol. I, pp. 152-154.
[31] Docket vol. I, p. 158.
[32] Docket vol. I, pp. 168-170.

These motions were granted by the Court in the Order dated December 9, 2015 and respondent SOF's Answer[33] was admitted. Respondent SOF alleged the following Special and Affirmative Defenses:

"**SPECIAL AND AFFIRMATIVE DEFENSES**

Respondent reiterates and re-pleads the preceding paragraphs of this Answer as part of his Special and Affirmative Defense.

The transfer of the two (2) parcels of land by Kingsville International Resources, Inc. (Kingsville) to Century Peak Property Development, Inc. (Century) is considered as a 'sale, barter or exchange of goods' subject to Value Added Tax (VAT).

14. Petitioners maintained that the transfer of the two (2) parcels of land from Kingsville to Century is not subject to VAT since it cannot be considered as a 'sale, barter or exchange of goods'.

15. Respondent differs. The transfer of the two (2) parcels of land is a transaction subject to VAT.

16. First, Kingsville is a corporation primarily engaged in the real estate business and the two (2) parcels of land were part of its stock in trade primarily for sale or for lease in the course of its trade or business. As stated in its Articles of Incorporation, its primary purpose is –

'To acquire by purchase, lease, donation or otherwise, and to own, use, improve, develop, subdivide, sell, mortgage, exchange, lease,

[33] Docket vol. I, pp. 178-186.

develop and hold for investment or otherwise, real estate of all kinds, whether improve, manage or otherwise dispose of buildings, houses, apartments and other structures of whatever kind together with their appurtenances.'

17. Section 106 of the National Internal Revenue Code (Tax Code) states:

SEC. 106. Value-Added Tax on Sale of Goods or Properties. –

(A) Rate and Base of Tax. – **There shall be levied, assessed and collected on every sale, barter or exchange of goods or properties**, value-added tax equivalent to [twelve percent (12%)] of the gross selling price or gross value in money of the goods or properties sold, bartered or exchanged, such tax to be paid by the seller or transferor.

(1) **The term 'goods' or 'properties'** shall mean all tangible and intangible objects which are capable of pecuniary estimation and shall include:

(a) Real properties held primarily for sale to customers or held for lease in the ordinary course of trade or business;

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(Emphasis supplied).

18. More importantly, the alleged Deed of Assignment is clear. There was an exchange of property between Kingsville and Century. It states:

For and in consideration of the full payment of KINGSVILLE's total subscription of Four Hundred Fifty Thousand (450,000) shares at One Hundred Pesos (P100.00) per share in capital stock of CENTURY PEAK PROPERTY DEVELOPMENT INC., a corporation that is now in the process of incorporation under the laws of the Republic of the Philippines, **KINGSVILLE hereby assigns, transfers and conveys unto CENTURY PEAK PROPERTY DEVELOPMENT, INC. all its rights titles and ownership** over the following properties consisting of:

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With the assignment and transfer of all rights, title and ownership of KINGSVILLE over the above-described parcels of land unto CENTURY PEAK PROPERTY DEVELOPMENT INC., the latter shall assume all obligations over the above described parcels of land in favor of KINGSVILLE as assignor.

(Emphasis supplied).

19. Clearly, there was an exchange of property between Kingsville and Century; that is the two (2) parcels of land in exchange for four hundred fifty thousand (450,000) shares.

20. Thus, there being a transfer of absolute ownership of the parcels of land held primarily for sale from Kingsville to Century, the transaction is subject to VAT pursuant to the clear provisions of the Tax Code.

**Revenue Regulation No.
4-2007 is inapplicable.**

21. Petitioner argued that Revenue Regulations No. 4-2007 (RR 4-07) is applicable since it was the prevailing regulation at the time of the execution of the alleged Deed of Assignment.

22. Respondent disagrees.

23. Section 4-106-8 of RR 4-07 states:

Section 8. CHANGE OR CESSATION OF STATUS AS VAT REGISTERED PERSON. - Sec. 4.106-8 of RR No. 16-2005 is hereby amended to read as follows:

SEC. 4.106-8. Change or Cessation of Status as VAT-registered Person.

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(b) Not subject to output tax

The VAT shall not apply to goods or properties existing as of the occurrence of the following:

(1) Change of control of a corporation by the acquisition of the controlling interest of such corporation by another stockholder or group of stockholders. The goods or properties used in business or those comprising the stock-in-trade of the corporation, having a change in corporate control, will not be considered sold, bartered or exchanged despite the change in the ownership interest in the said corporation.

Illustration: Abel Corporation is a merchandising concern and has an inventory of goods for sale amounting to Php 1 million. Nel Corporation, a real estate developer, exchanged its real estate properties for the shares of stocks of Abel Corporation resulting to the acquisition of corporate control. The inventory of goods owned by Abel Corporation (Php 1 million worth) is not subject to output tax despite the change in corporate control because the same corporation still owns them. This is in recognition of the separate and distinct personality of the corporation from its stockholders. However, the exchange of real estate properties held for sale or for lease, for shares of stocks, whether resulting to

> corporate control or not, is subject to VAT, subject to exceptions provided under Section 4.106-3 hereof. **On the other hand, if the transferee of the transferred real property by a real estate dealer is another real estate dealer, in an exchange where the transferor gains control of the transferee-corporation, no output VAT is imposable on the said transfer.**

24. In the first place, there was no change of control of a corporation to speak of. As admitted by petitioners, at the time of the taxable event (13 October 2010), there was no Century to speak of since the Securities and Exchange Commission (SEC) only issued the Certificate of Incorporation on 21 December 2010. Thus, there was nothing to gain control of.

25. Second, the provision being invoked by petitioner clearly intended that there be two (2) corporations already in existence. The requirement that the transferee and the transferor need to be a real estate dealer bolsters this argument.

26. It is elementary that a corporation only gains its juridical personality upon the approval of its corporate papers by the Securities and Exchange Commission (SEC).

27. As here, Century was yet to be formed. Thus, at the time of the taxable event there was no other corporation to speak of.

28. Even assuming but definitely not conceding that Century is already in existence since it was in the process of incorporating, it was yet to be determined that it will engage in real estate business.

29. Thus, the requirements of Section 4-106-8 of RR 4-07 that there be a (1) corporation and (2) engaged in real estate business was never satisfied and thus, Section 4-106-8 of RR 4-07 finds no applicability whatsoever in the instant case." *gr*

On November 26, 2015, the Securities and Exchange Commission (SEC) approved the amendments to the Articles of Incorporation of petitioner Century Peak, such as, the amendment to its corporate name, which is now Century Peak Hotel Management and Development, Inc.[34]

The Pre-Trial Conference was set on February 4, 2016.[35] The Pre-Trial Brief for the Petitioner[36] was filed on January 28, 2016; while respondent CIR's Pre-Trial Brief[37] was filed on January 29, 2016 and respondent SOF's Pre-Trial Brief[38] was filed on February 2, 2016.

On February 19, 2016, the parties filed their Joint Stipulation of Facts and Issues[39]. This was approved and adopted by the Court in the Pre-Trial Order[40] issued on March 11, 2016, which also terminated the pre-trial.

During trial, petitioners presented their sole witness, Atty. Perseveranda A. Abrenica[41], the assisting lawyer of petitioner Kingsville at the time of the execution of the Deed of Assignment on October 13, 2010.

The Formal Offer of Documentary Evidence for the Petitioners[42] was filed on March 21, 2016. In the Resolution[43] dated April 25, 2016, the Court admitted petitioner's Exhibits "P-1", "P-1-a", "P-2", "P-3", "P-4", "P-5", "P-6", "P-7", "P-8", "P-9", "P-10", "P-11", "P-12", "P-13", "P-14", "P-15", "P-16", "P17", "P-18", "P-19", "P-20", "P-21", and "P-22".

During the hearing for the initial presentation of evidence for respondent, counsel for respondent CIR manifested that she has no witness to present.[44]

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[34] Par. 17, Surrounding Circumstances, Facts Stipulated, JSFI, docket vol. II, p. 539.
[35] Notice of Pre-Trial Conference, docket vol. I, p. 381.
[36] Docket vol. II, pp. 384-391.
[37] Docket vol. II, pp. 514-523.
[38] Docket vol. II, pp. 530-533.
[39] Docket vol. II, pp. 537-542.
[40] Docket vol. II, pp. 551-554.
[41] Minutes of the Hearing dated March 16, 2016, docket vol. II, p. 555; docket vol. II, pp. 392-404.
[42] Docket vol. II, pp. 558-564.
[43] Docket vol. II, pp. 665-666.
[44] Minutes of the Hearing dated June 22, 2016, p. 667.

Thereafter, respondent SOF filed his Memorandum[45] on July 19, 2016. On the other hand, petitioner's Memorandum[46] was filed on July 21, 2016. Then the Memorandum (For Respondent)[47] CIR was filed on August 2, 2016. Thus, in the Resolution[48] dated August 8, 2016, the instant case was declared submitted for decision.

THE ISSUES

The parties agreed that the main issues to be resolved by this Court are the following:[49]

A. Is the transaction covered by the Deed of Assignment of the two parcels of land executed on October 13, 2010 considered as "sale, barter, or exchange of property" subject to value added tax?

B. Is Revenue Ruling No. 4-2007 applicable to the transaction under the Deed of Assignment?

PETITIONERS' ARGUMENTS

Petitioners argue that pursuant to Sections 61 and 62 of the Corporation Code, the Deed of Assignment of the two (2) parcels of land was a pre-incorporation subscription contract. They contend that the interpretation of Section 106 of the National Internal Revenue Code (NIRC) of 1997, as amended, must be in line with Sections 61 and 62 of the Corporation Code. According to petitioners, the NIRC of 1997, as amended, does not impose any VAT on subscription of shares pursuant to the incorporation of a corporation-still-to-be-formed, regardless of the nature of the corporation, whether real estate dealer or not. Jr

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[45] Docket vol. II, pp. 668-681.
[46] Docket vol. II, pp. 683-703.
[47] Docket vol. II, pp. 713-721.
[48] Docket vol. II, p. 723.
[49] Issues Stipulated, JSFI, docket vol. II, p. 540.

Petitioners contend that the Deed of Assignment is not sale, but property payment in the form of capital of petitioner Kingsville in petitioner Century Peak. They aver that the assignment of the properties of Kingsville is not deemed to be a sales transaction but an investment in the company and should not be subject to VAT.

Moreover, petitioners argue that the Deed of Assignment contemplates a tax-free exchange. They reiterate that the transaction is in the form of a subscription agreement and not deemed sale.

Furthermore, petitioners allege that Revenue Ruling No. 4-2007 is applicable in this case. They assert that in the said Revenue Ruling the Bureau of Internal Revenue clarified that the transfer of properties in exchange of stocks to gain control of the corporation is not deemed sale, hence, not subject to VAT. Petitioners also contend that at the time of the execution of the Deed of Assignment on October 13, 2010, the prevailing ruling is BIR Revenue Regulations No. 4-2007, and therefore the Deed of Assignment is not subject to output VAT. They allege that the assailed BIR Certification Ruling SN. 014-2012 dated February 20, 2012 and the assailed Resolution dated July 4, 2015 of respondent SOF are not consistent with the law. Petitioners point out that the basis of the assailed BIR Certification Ruling is Revenue Regulations No. 10-2011, which removed the very portion in Revenue Regulations No. 4-2007.

RESPONDENTS' ARGUMENTS

Respondents argue that the transfer of the two parcels of land through a Deed of Assignment entered into by and between petitioners is considered a "sale, barter or exchange of goods" subject to VAT. They allege that petitioner Kingsville is a corporation primarily engaged in the real estate business and the two parcels of land which it assigned, transferred and conveyed to petitioner Century Peak were goods it held primarily for sale in the course of its trade and business. Respondents contend that pursuant to Section 106 of the NIRC of 1997, as amended, the transfer of property by and between the petitioners was a "sale, barter or exchange of goods or properties" subject to VAT.

Furthermore, respondents contend that Revenue Regulations No. 4-2007 is inapplicable in the present case. They aver that Section

4.106-8 of RR No. 4-07 speaks of a change of control of a corporation by the acquisition of the controlling interest of such corporation by another stockholder or group of stockholders. In other words, there has to be two (2) parties involved in the transaction. One is the corporation whose controlling interest is to be acquired and second, the stockholder or group of stockholders who will acquire the said controlling interest. Respondents point out that at the time of the execution of the Deed of Assignment, there was no corporation yet whose controlling interest is to be acquired by another stockholder or group of stockholders. When petitioner Kingsville acquired the 450,000 shares in the capital stock of petitioner Century Peak, the latter was still in the process of incorporation, hence, not yet a corporation to begin with. Thus, the requirement that both the transferee-corporation and the transferor-corporation must be engaged in the real estate business is not satisfied.

THE COURT'S RULING

The Court of Tax Appeals has jurisdiction to entertain the present case

While it was never raised as an issue, this Court deems it proper to determine its jurisdiction over the present case for it is settled that jurisdiction over the subject matter is fundamental for a court to act on a given controversy.

In the case of *The Philippine American Life and General Insurance Company v. The Secretary of Finance*,[50] the Supreme Court squarely ruled that it is the Court of Tax Appeals that has jurisdiction over an appeal of adverse ruling of the Secretary of Finance in the exercise of its power of review under Section 4 of the NIRC of 1997, as amended. The relevant portion of the said decision is quoted below:

> "Admittedly, there is no provision in law that expressly provides where exactly the ruling of the Secretary of Finance under the adverted NIRC provision is appealable to. **However, We find that Sec. 7(a)(1) of RA 1125, as amended, addresses the seeming gap**

[50] G.R. No. 210987, November 24, 2014, 741 SCRA 578.

in the law as it vests the CTA, albeit impliedly, with jurisdiction over the CA petition as 'other matters' arising under the NIRC or other laws administered by the BIR. As stated:

> **Sec. 7. Jurisdiction.** — The CTA shall exercise:
>
> a. Exclusive appellate jurisdiction to review by appeal, as herein provided:
>
> 1. Decisions of the Commissioner of Internal Revenue in cases involving disputed assessments, refunds of internal revenue taxes, fees or other charges, penalties in relation thereto, **or other matters** arising under the National Internal Revenue or other laws administered by the Bureau of Internal Revenue. (emphasis supplied)

Even though the provision suggests that it only covers rulings of the Commissioner, We hold that it is, nonetheless, sufficient enough to include appeals from the Secretary's review under Sec. 4 of the NIRC.

It is axiomatic that laws should be given a reasonable interpretation which does not defeat the very purpose for which they were passed. Courts should not follow the letter of a statute when to do so would depart from the true intent of the legislature or would otherwise yield conclusions inconsistent with the purpose of the act. This Court has, in many cases involving the construction of statutes, cautioned against narrowly interpreting a statute as to defeat the purpose of the legislator, and rejected the literal interpretation of statutes if to do so would lead to unjust or absurd results.

Indeed, to leave undetermined the mode of appeal from the Secretary of Finance would be an injustice to taxpayers prejudiced by his adverse rulings. To remedy this situation, We imply from the purpose of RA 1125 and its amendatory laws that

> **the CTA is the proper forum with which to institute the appeal.** This is not, and should not, in any way, be taken as a derogation of the power of the Office of President but merely as recognition that matters calling for technical knowledge should be handled by the agency or quasi-judicial body with specialization over the controversy. As the specialized quasi-judicial agency mandated to adjudicate tax, customs, and assessment cases, there can be no other court of appellate jurisdiction that can decide the issues raised in the CA petition, which involves the tax treatment of the shares of stocks sold." *(Emphasis supplied and citations omitted)*

In view of the foregoing, it is clear that this Court has jurisdiction to entertain the present case.

Transaction covered by the Deed of Assignment is not subject to Value-Added Tax

Both the BIR Certification Ruling[51] SN. 014-2012 dated February 20, 2012 and the assailed Resolution[52] dated July 14, 2015 ruled that the transfer of real properties in exchange of stocks is subject to VAT based on Section 106 of the NIRC of 1997, as amended, which reads:

> "SEC. 106. *Value-Added Tax on Sale of Goods or Properties.* –
>
> (A) *Rate and Base of Tax.* – There shall be levied, assessed and collected on every sale, barter or exchange of goods or properties, value-added tax equivalent to twelve percent (12%) of the gross selling price or gross value in money of the goods or properties sold, bartered or exchanged, such tax to be paid by the seller or transferor.
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[51] Exhibit "P-11", docket vol. II, pp. 615-620.
[52] Exhibit "P-10", docket vol. II, pp. 611-614.

(1) The term 'goods or properties' shall mean all tangible and intangible objects which are capable of pecuniary estimation and shall include:

(a) Real properties held primarily for sale to customers or held for lease in the ordinary course of trade or business;

(b) The right or the privilege to use patent, copyright, design or model, plan, secret formula or process, goodwill, trademark, trade brand or other like property or right;

(c) The right or the privilege to use in the Philippines of any industrial, commercial or scientific equipment;

(d) The right or the privilege to use motion picture films, tapes and discs; and

(e) Radio, television, satellite transmission and cable television time.

The term 'gross selling price' means the total amount of money or its equivalent which the purchaser pays or is obligated to pay to the seller in consideration of the sale, barter or exchange of the goods or properties, excluding the value-added tax. The excise tax, if any, on such goods or properties shall form part of the gross selling price.

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(B) *Transactions Deemed Sale.* – The following transactions shall be deemed sale:

(1) Transfer, use or consumption not in the course of business of goods or properties originally intended for sale or for use in the course of business;

(2) Distribution or transfer to:

(a) Shareholders or investors as share in the profits of the VAT-registered persons; or

(b) Creditors in payment of debt;

(3) Consignment of goods if actual sale is not made within sixty (60) days following the date such goods were consigned; and

(4) Retirement from or cessation of business, with respect to inventories of taxable goods existing as of such retirement or cessation." (*Emphasis supplied*)

Based on the foregoing, transfers of goods or properties originally intended for sale or for use in the course of business is a transaction deemed sale which is subject to 12% VAT.

In this case, respondents found that petitioner Kingsville is a corporation primarily engaged in the real estate business and the two parcels of land which it assigned, transferred and conveyed to petitioner Century Peak were presumably held primarily for sale or use in the course of its business. Thus, respondents ruled that the transfer of property by and between petitioners is considered a "sale, barter or exchange of goods or properties" subject to VAT.

However, it must be noted, that Section 106(B)(1) of the NIRC of 1997, as amended, states that the goods or properties transferred are "originally intended for sale or for use in the course of business". While petitioner Kingsville is a corporation primarily engaged in the real estate business, there is no proof that the subject two parcels of land it assigned to petitioner Century Peak in consideration of the 450,000 shares of stock are properties originally intended for sale or for use in the course of business.

In the assailed Resolution, respondent SOF merely presumed that those two properties were held for sale or use in the course of its business, to wit: gr

> "Being a real estate dealer, as represented by CENTURY, KINGSVILLE is engaged in the business of buying, developing, selling, exchanging real properties as principal, and its real properties are **presumably held for sale or use in the course of its business**. Thus, the position that the transfer by KINGSVILLE to CENTURY of real properties is not subject to value added tax finds no basis in the law." (*Emphasis supplied*)

Respondents failed to present any proof that these two parcels of land were part of petitioner Kingsville's inventory. Hence, the transaction covered by the Deed of Assignment is not a transaction deemed sale.

Moreover, an examination of the Deed of Assignment[53] of the two parcels of land would show that it is a pre-incorporation subscription contract pursuant to Section 61 and Section 62 of the Corporation Code. The pertinent part of the Deed of Assignment provides:

> "For and inconsideration of the full payment of KINGSVILLE's total subscription of **Four Hundred Fifty Thousand (450,000) shares at One Hundred Pesos (P100.00) per share** in capital stock of **CENTURY PEAK PROPERTY DEVELOPMENT INC.**, a corporation that is now in the process of incorporation under the laws of the Republic of the Philippines, **KINGSVILLE** hereby **assigns, transfers and conveys** unto **CENTURY PEAK PROPERTY DEVELOPMENT INC.** all its rights, titles, and ownership over the following properties, consisting of:
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> xxx xxx xxx
>
> With the assignment and transfer of all rights, title, and ownership of KINGSVILLE over the above-described parcels of land unto **CENTURY PEAK PROPERTY DEVELOPMENT INC.**, the latter shall assume all

[53] Exhibit "P-14", docket vol. II, pp. 631-634.

obligations over the above-described parcels of land in favor of KINGSVILLE as assignor."[54]

Section 61 and Section 62 of the Corporation Code read as follows:

"**Sec. 61.** ***Pre-incorporation subscription.*** – A **subscription for shares of stock of a corporation still to be formed** shall be irrevocable for a period of at least six (6) months from the date of subscription, unless all of the other subscribers consent to the revocation, or unless the incorporation of said corporation fails to materialize within said period or within a longer period as may be stipulated in the contract of subscription: *Provided*, That no pre-incorporation subscription may be revoked after the submission of the articles of incorporation to the Securities and Exchange Commission.

Sec. 62. ***Considering for stocks***. – Stocks shall not be issued for a consideration less than the par or issued price thereof. **Consideration for the issuance of stock may be any** or a combination of any two or more **of the following**:

1. Actual cash paid to the corporation;

2. **Property**, tangible or intangible, actually received by the corporation and necessary or convenient for its use and lawful purposes at a fair valuation equal to the par or issued value of the stock issued;

3. Labor performed for or services actually rendered to the corporation;

4. Previously incurred indebtedness by the corporation; *gr*

[54] Exhibit "P-14", docket vol. II, pp. 632-633.

5. Amounts transferred from unrestricted retained earnings to stated capital; and

6. Outstanding shares exchanged for stocks in the event of reclassification or conversion.

Where the consideration is other than actual cash, or consists of intangible property such as patents or copyrights, the valuation thereof shall initially be determined by the incorporators or the board of directors, subject to approval by the Securities and Exchange Commission.

Shares of stock shall not be issued in exchange for promissory notes or future service.

The same considerations provided for in this section, insofar as they may be applicable, may be used for the issuance of bonds by the corporation.

The issued price of no-par value shares may be fixed in the articles of incorporation or by the board of directors pursuant to authority conferred upon it by the articles of incorporation or the by-laws, or in the absence thereof by the stockholders at a meeting duly called for the purpose representing at least a majority of the outstanding capital stock." *(Emphases supplied)*

Considering that the subject transaction is in the nature of pre-incorporation stock subscription, it cannot be deemed as sale. In the case of *Delpher Trades Corporation and Delfin Pacheco vs. Intermediate Appellate Court and Hydro Pipes Philippines, Inc.*[55], the Supreme Court ruled:

"After incorporation, one becomes a stockholder of a corporation by subscription or by purchasing stock directly from the corporation or from individual owners thereof (Salmon, Dexter & Co. v. Unson, 47 Phil. 649, citing Bole v. Fulton [1912], 233 Pa., 609). In the case at bar, in

[55] G.R. No. L-69259, January 26, 1988.

exchange for their properties, the Pachecos acquired 2,500 original unissued no par value shares of stocks of the Delpher Trades Corporation. Consequently, the Pachecos became stockholders of the corporation by subscription. **'The essence of the stock subscription is an agreement to take and pay for original unissued shares of a corporation, formed or to be formed.'** (Rohrlich 243, cited in Agbayani, Commentaries and Jurisprudence on the Commercial Laws of the Philippines, Vol. III, 1980 Edition, p. 430) It is significant that the Pachecos took no par value shares in exchange for their properties.

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The 'Deed of Exchange' of property between the Pachecos and Delpher Trades Corporation **cannot be considered a contract of sale. There was no transfer of actual ownership interests** by the Pachecos **to a third party**. The Pacheco family **merely changed their ownership from one form to another. The ownership remained in the same hands**. xxx" *(Emphasis supplied)*

It must be noted that Section 105 of the NIRC of 1997, as amended, provides that any person who, in the course of trade or business, sells, barters, exchanges, leases goods or properties, is subject to VAT. The provision reads as follows:

"SEC. 105. *Persons Liable*. – **Any person who, in the course of trade or business, sells, barters, exchanges, leases goods or properties**, renders services, and any person who imports goods shall be subject to the value-added tax (VAT) imposed in Sections 106 to 108 of this Code.

The value-added tax is an indirect tax and the amount of tax may be shifted or passed on to the buyer, transferee or lessee of the goods, properties or services. This rule shall likewise apply to existing contracts of sale

> or lease of goods, properties or services at the time of the effectivity of Republic Act No. 7716.
>
> The phrase *'**in the course of trade or business**'* **means the regular conduct or pursuit of a commercial or an economic activity, including transactions incidental thereto, by any person** regardless of whether or not the person engaged therein is a non-stock, non-profit private organization (irrespective of the disposition of its net income and whether or not it sells exclusively to members or their guests), or government entity. xxx" *(Emphasis supplied)*

It is clear from the foregoing that a person is subject to VAT if he sells, barters, exchanges, leases goods or properties in the course of trade or business.

Moreover, in the case of *Commissioner of Internal Revenue vs. Magsaysay Lines, Inc., et al.*[56], the Supreme Court held that VAT is levied only on the sale, barter or exchange of goods or services by persons who engage in such activities, in the course of trade or business.

In this case, petitioner Kingsville is engaged in the real estate business. Its primary purpose, as stated in its Amended Articles of Incorporation[57], is as follows:

> "PRIMARY PURPOSE
>
> To acquire by purchase, lease, donation or otherwise, and to own, use, improve, develop, subdivide, sell, mortgage, exchange, lease, develop, and hold for investment or otherwise, real estate of all kinds, whether improve, manage or otherwise dispose of buildings, houses, apartments, and other structures of whatever kind together with their appurtenances."

[56] G.R. No. 146984, July 28, 2006.
[57] Exhibit "P-9", docket vol. II, p. 601.

The transfer of properties by petitioner Kingsville to petitioner Century Peak as covered by the Deed of Assignment was not done in the course of trade or business. Thus, the transaction is not subject to VAT.

Revenue Regulations No. 4-2007 is not applicable to this case.

Section 4.106-8 of Revenue Regulations No. 16-2005[58], as amended by Revenue Regulations No. 4-2007[59], provides that transfer of properties between two real estate dealers, in an exchange where the transferor gains control of the transferee-corporation, shall not be subject to output VAT. The provision reads as follows:

> "SEC. 4.106-8. *Change or Cessation of Status as VAT-registered Person.* –
>
> xxx xxx xxx
>
> (b) *Not subject to output tax*
>
> The VAT shall not apply to goods or properties existing as of the occurrence of the following:
>
> (1) Change of control of a corporation by the acquisition of the controlling interest of such corporation by another stockholder or group of stockholders. The goods or properties used in business or those comprising the stock-in-trade of the corporation, having a change in corporate control, will not be considered sold, bartered or exchanged despite the change in the ownership interest in the said corporation.

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[58] Consolidated Value-Added Tax Regulations of 2005, September 1, 2005.

[59] Amending Certain Provisions of Revenue Regulations No. 16-2005, As Amended, Otherwise Known as the Consolidated Value-Added Tax Regulations of 2005, February 7, 2007; Exhibit "P-15", docket vol. II, pp. 635-656.

> *Illustration*: Abel Corporation is a merchandising concern and has an inventory of goods for sale amounting to Php 1 million. Nel Corporation, a real estate developer, exchanged its real estate properties for the shares of stocks of Abel Corporation resulting to the acquisition of corporate control. The inventory of goods owned by Abel Corporation (Php 1 million worth) is not subject to output tax despite the change in corporate control because the same corporation still owns them. This is in recognition of the separate and distinct personality of the coloration from its stockholders. However, the exchange of real estate properties held for sale or for lease, for shares of stocks, whether resulting to corporate control or not, is subject to VAT, subject to exceptions provided under Section 4.106-3 hereof. On the other hand, if the transferee of the transferred real property by a real estate dealer is another real estate dealer, in an exchange where the transferor gains control of the transferee corporation, no output VAT is imposable on the said transfer.

(2) Change in the trade or corporate name of the business;

(3) Merger or consolidation of corporations. The unused input tax of the dissolved corporation, as of the date of merger or consolidation, shall be absorbed by the surviving or new corporation."

In the present case, the respective Articles of Incorporation of petitioners Kingsville[60] and Century Peak[61] indicate the purpose for which they were incorporated, *viz*:

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[60] Exhibit "9", docket vol. II, pp. 600-610.
[61] Exhibit "3", docket vol. II, pp. 566-579.

"PRIMARY PURPOSE

To acquire by purchase, lease, donation or otherwise, and to own, use, improve, develop, subdivide, sell, mortgage, exchange, lease, develop, and hold for investment or otherwise, real estate of all kinds, whether improve, manage or otherwise dispose of buildings, houses, apartments, and other structures of whatever kind together with their appurtenances."[62]

"**SECOND:** A. That the primary purpose of this corporation is

To engage, operate, hold or manage real estate business. To acquire by purchase, lease, donation or otherwise, to use, improve, develop, subdivide, sell, mortgage, exchange, lease, develop, and hold for investment or otherwise, real estate of all kinds, whether improved, managed or otherwise deal in or dispose of buildings, houses, apartments, townhouses, condominiums, and other structures of whatever kind together with the appurtenances or improvements found thereon."[63]

A "Real estate dealer", includes any person engaged in the business of buying, developing, selling, exchanging real properties as principal and holding himself out as a full or part-time dealer in real estate.[64] Hence, based on the Articles of Incorporation and the definition of "Real estate dealer" as provided under RR No. 16-2005, both petitioners are considered as real estate dealers.

However, as admitted by petitioners, at the time of the taxable event or on October 13, 2010, petitioner Century Peak has yet to be incorporated. This means that petitioner Century Peak has yet to gain its juridical personality when the Deed of Assignment was executed because it was only on December 21, 2010 that the SEC issued its

[62] Exhibit "9", docket vol. II, p. 601.
[63] Exhibit "P-3", docket vol. II, p. 567.
[64] Section 4.106-3, Revenue Regulations No. 16-2005.

Certificate of Incorporation[65]. Therefore, when petitioner Kingsville acquired the 450,000 shares in the capital stock of petitioner Century Peak, the latter was still in the process of incorporation, hence, not yet a corporation to begin with. Consequently, RR No. 4-07 is not applicable to this case.

In view of the foregoing, no value-added tax is imposable on the Deed of Assignment executed on October 13, 2010 between petitioners.

WHEREFORE, premises considered, the instant Petition for Review is **GRANTED**. Accordingly, the Bureau of Internal Revenue Certification Ruling SN. 014-2012 and the Department of Finance Resolution dated July 14, 2015 are hereby **REVERSED** and **SET ASIDE**.

SO ORDERED.

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Associate Justice

WE CONCUR:

CAESAR A. CASANOVA
Associate Justice

Catherine T. Manahan
CATHERINE T. MANAHAN
Associate Justice

[65] Exhibit "P-2", docket vol. II, p. 565.

ATTESTATION

I attest that the conclusions in the above Decision were reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Associate Justice
Chairperson

CERTIFICATION

Pursuant to Article VIII, Section 13 of the Constitution, and the Division Chairperson's Attestation, it is hereby certified that the conclusions in the above Decision were reached in consultation before the case was assigned to the writer of the opinion of the Court.

ROMAN G. DEL ROSARIO
Presiding Justice