Republic of the Philippines
COURT OF TAX APPEALS
Quezon City

SECOND DIVISION

FIRST MERIDIAN DEVELOPMENT, INC.,
Petitioner,

-versus-

CITY OF DAVAO and HON. RODRIGO S. RIOLA, in his official capacity as the City Treasurer of Davao City,
Respondents.

CTA AC No. 159
(RTC Civil Case No. 34,852-13)

Members:
CASTAÑEDA, JR., *Chairperson,* *and*
CASANOVA *JJ.*

Promulgated:
NOV 2 9 2016
1:05 p.m.

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DECISION

CASANOVA, *J.*:

Before this Court is a Petition for Review[1] filed by petitioner-First Meridian Development, Inc. on November 9, 2015, with respondents' Comment[2] filed on January 4, 2016. The Petition for Review prays for this Court to render judgment ordering respondents to refund or credit the amount of Four Hundred Fifty Six Thousand Three Hundred Ninety Four Pesos (P456,394.00), plus legal interest, representing the 0.55% local business taxes for the first and second quarters of 2011 which were allegedly erroneously and illegally collected on January 18, 2011 and April 25, 2011, respectively.

Petitioner is a corporation duly organized and existing under Philippines laws with principal office address at Legaspi Oil Compound Km. 9.5, Sasa, Davao City.[3] It may be served with notices and other processes through its counsel, Carag De Mesa Zaballero San Pablo & Abiera Law Offices, with office address at Suite 2602, 26th Floor, The Atlanta Centre, No. 31 Annapolis Street, Greenhills, San Juan City, Metro Manila.[4]

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[1] Docket, pp. 8-31.
[2] Ibid., pp. 144-158.
[3] Par. 11, The Parties, Petition for Review, Id., p. 11.
[4] Par. 11.2, The Parties, Petition for Review, Id.

Respondent-City of Davao is a local government unit (LGU) duly created by law, while co-respondent Hon. Rodrigo S. Ariola is being impleaded in his official capacity as the City Treasurer of Davao City. He is represented by Atty. Oscar Mata, Legal Officer of Davao City.[5]

Respondents City of Davao and City Treasurer may be served with summons, notices and other Court processes at City Hall Building, San Pedro Street, Davao City.[6]

The facts of the case, as culled from the records, are as follow:

In 2010, petitioner obtained the amount of One Hundred Sixty Five Million Nine Hundred Sixty One Thousand Four Hundred Fifty Eight and 25/100 Pesos (P165,961,458.25) from dividends on its San Miguel Corporation (SMC) Preferred Shares and interests on its money market placements, computed as follows:

Nature of Income	FMDI
Dividends	P163,989,405.00
Interest	1,972,053.25
Total	**P165,961,458.25**[7]

For the first half of the year 2011, respondent City of Davao, through respondent City Treasurer Riola, collected from petitioner the 0.55% local business taxes in the aggregate amount of P456,394.00 on the dividends derived from its SMC Preferred Shares and interests on money market placements. Petitioner paid the same under protest on January 18, 2011 and April 25, 2011.[8]

On September 13, 2012, petitioner filed with respondent City Treasurer its written administrative claim for refund or credit of the said local business taxes collected.[9]

Due to alleged inaction of the City Treasurer on its protest, petitioner filed a Petition for Review before the Regional Trial Court (RTC) of Davao City on January 17, 2013.[10]

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[5] Pars. 12 and 12.1, The Parties, Petition for Review, Id.
[6] Pars. 12.2, The Parties, Petition for Review, Id.
[7] Par. 16, Statement of Facts, Petition for Review, Id., p. 13.
[8] Par. 17, Statement of Facts, Petition for Review, Id., pp. 13-14.
[9] Par. 18, Statement of Facts, Petition for Review, Id., p. 14.
[10] Pars. 17 and 18, Statement of Facts, Petition for Review, Id.

On June 22, 2015, the RTC of Davao, Branch 16, promulgated its Decision[11] dismissing petitioner's Petition for Review, to wit:

> "**FOR REASONS STATED**, the instant 'Petition for Tax Refund or Credit Under Section 156, R.A. 7160' filed by the Petitioner is hereby **DENIED** and/or **DISMISSED.**
>
> **SO ORDERED.**"

Thus, petitioner filed a Motion for Reconsideration[12] on August 4, 2015, which was denied by the court *a quo* in an Order[13] dated September 11 2015.

Consequently, petitioner filed its Petition for Review[14] before the Court of Tax Appeals on November 9, 2015.

In a Resolution[15] dated November 24, 2015, the Court ordered respondents to file their comment, not a motion to dismiss, within ten (10) days from notice thereof. The same was complied[16] with by respondents on January 4, 2016.

Subsequently, in a Resolution[17] dated January 19, 2016, the Court gave the parties a period of thirty (30) days from notice thereof to submit their simultaneous memoranda. Upon receipt of the same, the instant petition shall be considered submitted for decision.

The Court submitted the instant case for decision in a Resolution[18] dated March 31, 2016, after taking into consideration petitioner's Memorandum[19] filed on February 22, 2016 and respondents' Memorandum[20] filed on March 14, 2016.

Hence, this Decision.

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[11] Annex "P-1" to the Petition for Review, Id, pp. 32- 41.
[12] Annex "P-7" to the Petition for Review, Id, pp. 72-88.
[13] Annex "P-2" to the Petition for Review, Id, p. 42.
[14] Supra note 1.
[15] Docket, p. 143.
[16] Ibid., pp. 144-158.
[17] Id., p. 161.
[18] Id., p. 213.
[19] Id., pp. 162-188.
[20] Id., pp. 195-211.

The sole issue raised by petitioner is whether or not petitioner is entitled to a refund or credit of the 0.55 % local business taxes collected for the first and second quarters of 2011 on the dividends received from its SMC preferred shares and interest on its money market placements for the taxable year 2010.

In support of the foregoing issue, petitioner argues that it is erroneous and illegal for respondents to assess a 0.55% local business tax on the dividends and interest income of a taxpayer which is a non-bank or a financial institution pursuant to Section 133 (a) of Republic Act No. 7160 (R.A. No. 7160) on the following grounds: (i) that its Amended Articles of Incorporation indicates that it is a holding company, which acquires and holds all types of properties, including real properties and not only shares of stock or other evidences of indebtedness; (ii) that its primary purpose states that it is expressly prohibited from acting as an investment company or a securities broker and/or dealer, which are all types or classifications of a non-bank financial intermediary; (iii) that it is not engaged in lending money, investing, reinvesting or trading of securities and/or foreign exchange either for its own account or for the account of others in a regular or recurring basis. It merely places its own money in banks or other securities; (iv) that it was not required by the Securities and Exchange Commission to secure a secondary license, or regulated by the Bangko Sentral ng Pilipinas or by the Insurance Commission; (v) that petitioner and other holding companies funded by the coconut levy funds were organized solely to hold SMC shares and have not engaged in any business activity; and, (vii) that its money market placements were merely incidental to its ownership of said shares and not because it is engaged in trade or commercial activity as a means of livelihood.

By way of comment, respondents argue that petitioner is deemed "a bank and other financial institution", specifically, a "non-bank financial intermediary or an investment company", by virtue of its investment and money placements in San Miguel Corporation; that the business purpose of petitioner as contained in its Amended Articles of Incorporation is wittingly and unwittingly broad enough to catch all the descriptive function of a non-bank financial intermediary as provided under Section 4101Q.1 of the Manual of Regulations for Non-Bank Financial Institutions issued by the Bangko Sentral ng Pilipinas; that petitioner's Articles of Incorporation which states that it shall not act as investment company or securities broker or dealer is not a conclusive proof that it is not a bank or other financial institution; that being a stock corporation, petitioner is presumed to have been organized to engage in business with the end view of a profit; that the definition of gross sales/receipts under Section 131(n) of R.A. No. 7160 does not include dividends and interest income as component of sales or receipts; that the opinion of the Bureau of Local Government Finance that petitioner is exempt from local business tax for not being a bank and other financial institution, is not binding upon the issue involved in this case, as it is not an administrative agency whose findings on question of facts and law are given weight and respects in the courts; and, the ruling of the Supreme Court in COCOFED vs. Republic is not squarely applicable as the same did not delve on the taxability of the fund or income, but solely on the public nature of the fund.

The Petition for Review is bereft of merit.

Section 133 (a) of the LGC explicitly withholds from any local government units, i.e., whether the province, city, municipality, or barangay, the power to levy tax on income, except when levied on banks and financial institutions.[21]

In this case, respondents assessed petitioner for local business taxes for the first half of the taxable year 2011 on its gross receipts derived from dividends it received from SMC Preferred Shares and interest income on its money market placements earned in taxable year 2010, pursuant to Section 69 (f) of Davao City Ordinance No. 158-05, to wit:

> "Section 69. **Imposition of Tax.**— There is hereby imposed on the following persons who establish, operate, conduct or maintain their respective business within the City a graduated business tax in the amounts hereafter prescribed:
>
> x x x x
>
> (f) **On Banks and Other Financial Institutions**, at the rate of fifty-five percent (55%) of one percent (1%) of the gross receipts of the preceding calendar year derived from **interest**, commissions and discounts from lending activities, income from financial leasing, **dividends**, rentals on property, and profit from exchange or sale of property,

[21] **Section 133.** *Common Limitations on the Taxing Powers of Local Government Units.* - Unless otherwise provided herein, the exercise of the taxing powers of provinces, cities, municipalities, and barangays shall not extend to the levy of the following:

(a) Income tax, except when levied on banks and other financial institutions;

insurance premium. All other income and receipts not herein enumerated shall be excluded in the computation of the tax."

Such provision is pattered from Section 143 (f) of the LGC, which reads:

"SEC. 143. Tax on Business.— The municipality may impose taxes on the following businesses:

(a) x x x x

x x x x

(f) On banks and other financial institutions, at a rate not exceeding fifty percent (50%) of one percent (1%) on the gross receipts of the preceding calendar year derived from interest, commissions and discounts from lending activities, income from financial leasing, dividends, rentals on property, and profit from exchange or sale of property, insurance premium.

x x x x."

However, both Section 131 (e)[22] of the LGC and Section 5(b3) of Ordinance No. 15-05[23] failed to give a precise definition of what constitutes a "bank and other financial institutions". In fact, it merely describes such concept by enumerating those entities that may fall within such term, *i.e.*, **non-bank financial intermediaries**, lending investors, finance and investment companies, pawnshops, money shops, and insurance companies. Thus, We must look on the definition of the same under other provisions of law or rules and regulations.

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[22] "SECTION 131. Definition of Terms.- When used in this Title, the term:

x x x x

(e) 'Banks and other financial institutions' include non-bank financial intermediaries, lending investors, finance and investment companies, pawnshops, money shops, insurance companies, stock markets, stock brokers and dealers in securities and foreign exchange, as defined under applicable laws, or rules and regulations thereunder;"

[23] SECTION 5. Definition of Terms. —

x x x x

(b3) Banks and other financial institutions. — include non-bank financial intermediaries, lending investors, finance and investment companies, pawnshops, money shops, insurance companies, stock markets, stock brokers and dealer in securities and foreign exchange, as defined under applicable laws, or rules and regulations thereunder;

Section 2.3 of Revenue Regulations (RR) No. 9-2004, issued on June 21, 2004, by the Bureau of Internal Revenue, defines "non-bank financial intermediaries" in the following manner:

> "2.3. Non-bank Financial Intermediaries — shall refer to persons or entities **whose principal functions include** the lending, **investing or placement of funds or evidences of indebtedness or equity deposited with them, acquired by them or otherwise coursed through them, either for their own account or for the account of others.** This includes all entities regularly engaged in the lending of funds or purchasing of receivables or other obligations with funds obtained from the public through the issuance, endorsement or acceptance of debt instruments of any kind for their own account, or through the issuance of certificates of assignment or similar instruments with recourse, trust certificates, or of repurchase agreements, whether any of these means of obtaining funds from the public is done on a regular basis or only occasionally." (Emphasis supplied)

Such concept was further expounded in Section 4101Q.1 of the Manual of Regulations for Non-Bank Financial Institutions in this wise:

> "§ 4101Q.1 **Financial Intermediaries**. Financial intermediaries shall mean persons or entities whose **principal functions** include the lending, **investing or placement of funds or evidences of indebtedness or equity deposited with them, acquired by them, or otherwise coursed through them either for their own account or for the account of others.**
>
> **Principal** shall mean chief, main, most considerable or important, of first importance, leading, primary, foremost, dominant or preponderant, as distinguished from secondary or incidental.
>
> **Functions** shall mean actions, activities or operations of a person or entity by which his/its business purpose is fulfilled or carried out. The business or purpose of a person or entity may be determined from the purpose clause in its articles of incorporation/partnership, and from the nature of the business indicated in his/its application for

> registration of business filed with the appropriate government agency.
>
> To be considered a financial intermediary, a person or entity must perform any of the following functions on a regular and recurring, not on an isolated basis:
>
> a. Receive funds from one (1) group of persons, irrespective of number, through traditional deposits, or issuance of debt or equity securities; and make available/lend these funds to another person or entity, and in the process acquire debt or equity securities;
>
> b. Use principally the funds received for acquiring various types of debt or equity securities;
>
> c. Borrow against, or lend on, or buy or sell debt or equity securities;
>
> d. Hold assets consisting principally of debt or equity securities such as promissory notes, bills of exchange, mortgages, stocks, bonds, and commercial papers;
>
> e. Realize regular income in the nature of, but need not be limited to, interest, discounts, capital gains, underwriting fees, guarantees, fees, commissions, and service fees, principally from transactions in debt or equity securities or by being an intermediary between suppliers and users of funds."

Petitioner argues that its business does not fall within the foregoing definitions of "Non-Bank Financial Intermediaries" on account of the following: (i) that its Amended Articles of Incorporation indicates that it is a holding company; (ii) that its primary purpose states that it is expressly prohibited from acting as an investment company or a securities broker and/or dealer; (iii) that it was not required by the Securities and Exchange Commission to secure a secondary license; and, (iv) that it is not regulated by the Bangko Sentral ng Pilipinas or by the Insurance Commission.

To check the veracity of the foregoing arguments, it is important to look into petitioner's primary purpose, as indicated in its Amended Articles of Incorporation, *viz:*

"<u>PRIMARY PURPOSE</u>

> The primary purpose for which such Corporation is formed is:
>
> > To purchase, subscribe for, or otherwise acquire and own, hold, use, sell, assign, transfer, mortgage, pledge, exchange, or otherwise dispose of real and personal property of every kind and description , including shares of stock, voting trust certificates for shares of the capital stock, bonds, debentures, notes, evidences of indebtedness, and other securities, contracts, or obligations of any corporation or corporations, association or associations, domestic or foreign, and to pay therefor in whole or in part in cash or by exchanging therefor stocks, bonds, or other evidences of indebtedness or securities, contracts, or obligation, to receive, collect, and dispose of the interest, dividends and income arising from such property, and to possess and exercise in respect thereof, all the rights, powers and privileges of ownership, including all voting powers on any stocks so owned; and to do every act and thing covered generally by the denomination 'holding corporation', and especially to direct the operations of other corporations through the ownership of stock therein, provided however that the Corporation shall not act as an investment company or a securities broker and/or dealer nor exercise the functions of a trust corporation."

A careful analysis of the nature of petitioner's business in line with the foregoing definitions of non-bank financial intermediaries shows that its primary purpose is extensive enough to cover most of the principal functions of a non-bank financial intermediary.

Further, the self-imposed prohibition in the last phrase of petitioner's primary purpose in its Articles of Incorporation which states that "it shall not act as an investment company or a securities broker and/or dealer nor exercise the functions of a trust corporation" cannot prevail over the real nature of transaction undertaken by petitioner, which is mainly investing or placement of funds. It cannot also guarantee that petitioner will not undertake/ engage in any of the said activities. Verily, by actually engaging in the business of stock investment and money market placements in SMC, the said proviso was negated and should, therefore, be disregarded. Thus, this Court finds no cogent reason to set aside the following findings and conclusions of the court a quo, to which We fully agree, to wit:

> "While the primary purpose of Petitioner appears to set a qualification or condition that: **'provided however that the Corporation shall not act as an investment company or a securities broker and/or dealer nor exercise the functions of a trust corporation,'** said **proviso** in the Court's mind is a classic evasion by Petitioner from the requirement to secure a secondary license for investment company under the regulation of the Bangko Sentral nf Pilipinas for non-banking financial intermediaries, per second paragraph of **Section 4101Q1 of MANUAL OF REGULATIONS FOR NON-BANK FINANCIAL INSTITUTIONS,** to wit:
>
> > 'Non-banking financial intermediaries shall include the following:
> >
> > (1) **A person or entity licensed and/or registered with any government regulatory body as a non-bank financial intermediary, such as investment house, investment company, financing company, securities dealer/broker, lending investor, pawnshop, money broker, fund manager, cooperative, insurance company, non-stock savings and loan association and building and loan association**. (underscoring supplied).
> >
> > x x x x'
>
> Petitioner cannot hide under the cloak of its evasive proviso, because Petitioner is glaringly and clearly under the category of a Financial Intermediary.
>
> To stress, the income of the Petitioner comes only from two sources, to wit:

> 1. **Dividends from FMDI's SMC Shares; and**
> 2. **Interest Income from FMDI's Money Market Placements** (Par. 11, Petition)
>
> In short, these **dividends and interests** are not considered incidental to its business quest, but are the **principal** (defined above as: **Principal** shall mean chief, main, most considerable or important, of first importance, leading, primary, foremost, dominant or preponderant, as distinguished from secondary or incidental) incomes of Petitioner's Corporation in the regular course of its business in line with the Primary Purpose of its Amended Articles of Incorporation."

Lastly, petitioner, being a stock corporation, is reasonably expected to perform all the above-enumerated functions in its Amended Articles of Incorporation with the end view of earning profits. Thus, any profits which it receives whether in the form of dividends or interest income, cannot be considered as mere incidental to its business, but a direct consequence of its business engagements as a non-bank financial intermediary.

Accordingly, based on the foregoing definition of non-bank financial intermediary and petitioner's acts of investing in equity securities, holding of assets consisting of shares of stocks and placement of funds on a regular and recurring basis explicitly affirms the conclusion that petitioner is a non-bank financial intermediary whose income may, therefore, be subjected to business tax under Section 143 (f) of the LGC of 1991, as amended.

WHEREFORE, premises considered, the Petition for Review is **DENIED** for lack of merit.

SO ORDERED.

CAESAR A. CASANOVA
Associate Justice

I CONCUR:

JUANITO C. CASTAÑEDA, JR.
Associate Justice

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.
Associate Justice
Chairperson, Second Division

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