REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

THIRD DIVISION

ROCK STEEL RESOURCES, 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. 158

Members:

BAUTISTA, *Chairperson*
FABON-VICTORINO, and
RINGPIS-LIBAN, *JJ.*

Promulgated:

MAR 16 2017
11:30 a.m.

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DECISION

***Fabon-Victorino, J.*:**

This Petition for Review[1] filed by Rock Steel Resources, Inc. (RSRI) pursuant to Section 7(a)(3) of Republic Act (RA) No. 1125, as amended, seeks to reverse and set aside the Decision[2] dated June 22, 2015 and Order[3] dated September 11, 2015 of the Regional Trial Court (RTC), Branch 16, Davao City in Civil Case No. 34,855-13, entitled Rock Steel Resources, Inc. v. City of Davao and Hon. Rodrigo S. Riola, in his official capacity as the City Treasurer of Davao City. The assailed Decision denied petitioner RSRI's claim for refund of local business tax alleged to have been erroneously and illegally levied and collected on the dividends and interest it received from San Miguel Corporation in 2010.

First, the facts.

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[1] Docket, pp. 8-30.
[2] Annex "P-1", Petition for Review, docket, pp. 32-41; RTC Records, pp. 337-346.
[3] Annex "P-2", Petition for Review, docket, p. 42; RTC Records, p. 375.

Petitioner is a domestic corporation, with principal office address at Legaspi Oil Compound Km. 9.5, Sasa, Davao City.[4] It was incorporated on August 12, 1983 with the following primary purpose, as enumerated in its Amended Articles of Incorporation:

> 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 other securities, contracts, or obligations, 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.[5]

On the other hand, respondent City of Davao is a local government unit (LGU) created by law, while respondent

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[4] Par. 11, The Parties, Petition for Review, docket, p. 11; Annexes "P-9" and "P-10", docket, pp. 89-101 and 102-113; Annexes "D" and "D-1", Petition, RTC Records, pp. 61-73 and 74-85.

[5] Annexes "P-9" and "P-10", Petition for Review, docket, pp. 89-101 and 102-113; Annexes "D" and "D-1", RTC Records, pp. 61-73 and pp. 74-85.

Rodrigo S. Riola is its City Treasurer. Both have office address at City Hall Building, San Pedro Street, Davao City.[6]

Petitioner was one of the fourteen (14) holding companies formed by the Coconut Industry Investment Fund (CIIF) in 1983 for the purpose of owning and holding shares of stock of San Miguel Corporation (SMC). In 1986, the said 14 holding companies were sequestered by the Philippine Commission on Good Government (PCGG). Various cases were subsequently filed to determine the ownership of the 14 holding companies and the SMC shares of stock held by them.

In October 2009, the 58,237,403 SMC common shares of stock held by petitioner were converted into equal number of preferred shares upon approval thereof by the Supreme Court *En Banc.* The dividends received by petitioner from its SMC preferred shares were deposited in a trust account that earned interest from money market placements.

In 2010, petitioner received dividends of ₱441,917,103.62 from its SMC preferred shares of stock, and interests from its money market placements, computed as follows:[7]

NATURE	AMOUNT
Dividends	₱ 436,780,522.50
Interest	5,136,581.12
TOTAL	**₱441,917,103.62**

For the first half of 2011, respondent City of Davao, through respondent City Treasurer Riola, collected from petitioner local business tax at the rate of 0.55% on the foregoing dividends and interest in the aggregate amount of ₱1,215,272.00, computed as follows:

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[6] Par. 12 and 12.1, The Parties, Petition for Review, docket, p. 11.
[7] Par. 16, Statement of Facts, Petition for Review, docket, p. 13.

Period Covered	Date of Payment	Official Receipt No.	Amount
January - March 2011	1/18/2011	5791184A	₱ 607,636.00
April - June 2011	4/25/2011	9884254A	607,636.00
TOTAL			**₱1,215,272.00**

On September 13, 2012, petitioner filed with respondent City Treasurer an administrative claim for refund or credit of the amounts paid under protest claiming that they were erroneously and illegally levied and collected.[8]

On January 17, 2013, petitioner filed a Petition for Refund or Credit with the RTC of Davao City on the ground of inaction on part of respondent City Treasurer to toll the running of the two-year prescriptive period mandated in Section 196 of RA No. 7160, otherwise known as the Local Government Code (LGC).[9]

On June 22, 2015, the RTC rendered the assailed Decision denying petitioner's Petition for Refund or Credit, as follows:

> **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**.

The RTC considered petitioner as a financial intermediary pursuant to Section 4101Q.1 of the Manual of Regulations for Non-Bank Financial Institutions issued by the *Bangko Sentral ng Pilipinas* (BSP), hence, the dividends derived from its SMC preferred shares and the interest on its money market placements are subject to local business tax under Section 143(f) of the LGC.

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[8] Annex "P-5", Petition for Review, docket, pp. 45-54; Annex "B", RTC Records, pp. 22-31.
[9] Annex "P-6", Petition for Review, docket, pp. 55-71; RTC Records, pp. 3-19.

In the similarly assailed Order dated September 11, 2015, the RTC denied petitioner's Motion for Reconsideration.

Hence, the present action filed on November 9, 2015, with the lone issue, as follows:

> 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 FROM ITS SMC PREFERRED SHARES AND INTEREST ON ITS MONEY MARKET PLACEMENTS FOR TAXABLE YEAR 2010.

In its Memorandum, petitioner submits that it is entitled to a refund or credit of the local business tax it paid under protest on the following grounds: (A) local government units are expressly prohibited from imposing income tax under Section 133(a) of the LGC, unless it is levied on banks and other financial institutions; (B) petitioner is neither a bank nor a non-bank financial institution, nor one engaged in business that is subject to local business tax under Section 143 of the LGC; and (C) petitioner's income partakes the nature of public funds, thus, business tax cannot be imposed on it.

Respondent however argues that petitioner is deemed a non-bank financial intermediary on account of its stock investments and money placements in SMC. It is an entity expressly included in the definition of banks and other financial institution. Besides, its business purpose per its Articles of Incorporation is so broad as to include all the descriptive functions of a non-bank financial intermediary provided under Section 4101Q.1 of the Manual of Regulations for Non-Bank Financial Institutions issued by the BSP. As a stock corporation, it is deemed organized to engage in stock investments and money placements to realize profit. Thus, as a non-bank financial intermediary, petitioner is subject to local business tax pursuant to Section 143(f) of the LGC, on its gross receipts consisting of dividends and interest. Even assuming that petitioner's SMC shares are deemed

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government property, the income derived therefrom is not covered by the prohibition on taxing government property under Section 133 of the LGC.

THE COURT'S RULING

The instant petition is impressed with merit.

The Constitution itself empowers local government units (LGUs) to create their own sources of revenues and to levy taxes, fees, and charges subject to such guidelines and limitations as the Congress may provide, consistent with the basic policy of local autonomy.[10] Such power of the LGUs to tax is however subject to the limitations enumerated in Section 133(o) of the LGC,[11] which proscribes imposition of taxes, fees or charges of any kind on the National Government, its agencies and instrumentalities.

To be sure, the present case is not the first on the matter. Several cases involving SMC shares held by holding companies created in 1983 by the Coconut Industry Investment Fund (CIIF) had been filed in various courts. The issue of ownership and taxability of such SMC shares have been punctuated in the case of *Philippine Coconut Producers Federation, Inc. (COCOFED) vs. Republic of the Philippines*[12], wherein the Supreme Court categorically declared that the SMC shares, such as the subject of the present case, are owned by the government, *viz*:

> **The CIIF Companies and the CIIF Block of SMC shares are public funds/assets**
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> **From the foregoing discussions, it is fairly established that the coconut levy funds are special public funds. Consequently, any property purchased**

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[10] Section 5, Article X, 1987 Philippine Constitution.

[11] *Philippine Fisheries Development Authority (PFDA) vs. Central Board of Assessment Appeals, et al.*, G.R. No. 178030, December 15, 2010.

[12] G.R. Nos. 177857-58 and 178193, January 24, 2012.

by means of the coconut levy funds should likewise be treated as public funds or public property, subject to burdens and restrictions attached by law to such property.

In this case, the 6 CIIF Oil Mills were acquired by the UCPB using coconut levy funds. On the other hand, the 14 CIIF holding companies are wholly owned subsidiaries of the CIIF Oil Mills. Conversely, these companies were acquired using or whose capitalization comes from the coconut levy funds. However, as in the case of UCPB, UCPB itself distributed a part of its investments in the CIIF oil mills to coconut farmers, and retained a part thereof as administrator. The portion distributed to the supposed coconut farmers followed the procedure outlined in PCA Resolution No. 033-78. And as the administrator of the CIIF holding companies, the UCPB authorized the acquisition of the SMC shares. In fact, these companies were formed or organized solely for the purpose of holding the SMC shares. As found by the Sandiganbayan, the 14 CIIF holding companies used borrowed funds from the UCPB to acquire the SMC shares in the aggregate amount of P1.656 Billion.

Since the CIIF companies and the CIIF block of SMC shares were acquired using coconut levy funds – funds, which have been established to be public in character – it goes without saying that these acquired corporations and assets ought to be regarded and treated as government assets. Being government properties, they are accordingly owned by the Government, for the coconut industry pursuant to currently existing laws.

It may be conceded hypothetically, as COCOFED *et al.* urge, that the 14 CIIF holding companies acquired the SMC shares

> in question using advances from the CIIF companies and from UCPB loans. But there can be no gainsaying that the same advances and UCPB loans are public in character, constituting as they do assets of the 14 holding companies, which in turn are wholly-owned subsidiaries of the 6 CIIF Oil Mills. And these oil mills were organized, capitalized and/or financed using coconut levy funds. **In net effect, the CIIF block of SMC shares are simply the fruits of the coconut levy funds acquired at the expense of the coconut industry. In *Republic v. COCOFED*, the en banc Court, speaking through Justice (later Chief Justice) Artemio Panganiban, stated: Because the subject UCPB shares were acquired with government funds, the government becomes their prima facie beneficial and true owner. By parity of reasoning, the adverted block of SMC shares, acquired as they were with government funds, belong to the government as, at the very least, their beneficial and true owner.** *(Emphasis supplied)*

Since the subject shares are government owned, it logically follows that the dividends and any income derived therefrom belong to and are owned by the government as well. That being the case, the subject SMC shares and the dividends and any income derived therefrom are beyond the taxing power of respondent City of Davao pursuant to Section 133(o) of the LGC of 1991. Evidently, it was erroneous on the part of respondent City of Davao to have levied and collected local business tax at the rate of 0.55% on the dividends arising from petitioner's SMC preferred shares and interests on money market placements.

Even assuming that petitioner and its SMC shares are within the taxing power of respondent City of Davao, petitioner is still not liable for business tax imposed by virtue of Section 143(f) of the LGC, in relation to Section 151 of the same Code, which grants to a city the power to impose taxes on banks and other financial institutions. The cited provisions are hereby quoted for easy reference, thus:

> SEC. 143. *Tax on Business.* – **The municipality may impose taxes on the following businesses**:
>
> xxx xxx xxx
>
> (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.
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> xxx xxx xxx
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> SEC. 151. *Scope of Taxing Powers.* – Except as otherwise provided in this Code, **the city, may levy the taxes, fees, and charges which the province or municipality may impose**: xxx
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> **The rates of taxes that the city may levy may exceed the maximum rates allowed for the province or municipality by not more than fifty percent (50%)** except the rates of professional and amusement taxes. *(Emphases supplied)*

The term "banks and other financial institutions" is defined under Section 131(e) of the LGC, as follows:

> SEC. 131. *Definition of Terms.* – When used in this Title, the term:
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> xxx xxx xxx

> (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**; *(Emphasis supplied)*

While Section 131(e) of the LGC of 1991 includes "non-bank financial intermediaries" in the term "banks and other financial institutions," it does not define the term "non-bank financial intermediaries" but suggested resort to other applicable laws, or rules and regulations for such definition is allowed.

In this regard, Section 22(W) of the National Internal Revenue Code (NIRC) of 1997, as amended, defines the term "non-bank financial intermediary", as follows:

> (W) The term *"non-bank financial intermediary"'* means a financial intermediary, as defined in Section 2(D)(c) of Republic Act No. 337, as amended, otherwise known as the General Banking Act, **authorized by the Bangko Sentral ng Pilipinas (BSP) to perform quasi-banking activities.** *(Emphasis supplied)*

On the other hand, Section 2(D)(c) of R.A. No. 337, otherwise known as the General Banking Act, as amended by Presidential Decree (P.D.) No. 71, defines financial intermediaries as follows:

> Sec. 2-D. For purposes of Sections Two, Two-A, Two-B, and Two-C the following definition or terms shall apply:
>
> xxx xxx xxx

> (c) "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;

In Section 2.3 of Revenue Regulations (RR) No. 9-2004, the BIR 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)*

A more elaborate definition of the term financial intermediaries is found in Section 4101Q.1 of the Manual of Regulations for Non-Bank Financial Institutions, thus:

> **§ 4101Q.1** ***Financial intermediaries***
> *Financial intermediaries* shall mean persons or entities whose **principal functions**

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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 or 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.
>
> **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.
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> (2) A person or entity which holds itself out as a non-banking financial intermediary, such as by the use of a business name, which includes the term *financing, finance, investment, lending* and/or any word/phrase of similar import which connotes financial intermediation, or an entity which advertises itself as a financial intermediary and is engaged in the function(s) where financial intermediation is implied.
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> (3) **A person or entity performing any of the functions enumerated in Items *a* to *e* of this Subsection.** *(Emphasis supplied)*

From the foregoing definitions, a local government unit such as respondent Davao City, can impose business tax only on banks and other financial institutions pursuant to Section 143(f) of the LGC of 1991, which includes non-bank financial intermediaries, based on Section 131(e) of the LGC.

In the instant case, petitioner was assessed for local business tax on the premise that it is a non-bank financial intermediary. However, respondents failed to present any credible and convincing proof that petitioner is a financial intermediary or has even engaged in the activities of a financial institution/intermediary as enumerated or defined in the above-quoted laws, and rules and regulations.

In fact, there is no indication that petitioner was authorized by the BSP to perform quasi-banking activities as a non-bank financial intermediary pursuant to Section 22(W) of the NIRC of 1997, as amended, and Section 2(D)(c) of R.A. 337, or the General Banking Act, as amended.

In this regard, Section 4 of R.A. No. 337, as amended by P.D. No. 1828, states that the authority to determine whether a person or an entity is (a) performing banking or quasi-banking functions, or (b) engaged in other types of financial intermediation, is vested on the Monetary Board subject to judicial review, thus:

> Sec. 4. The determination of whether a person or an entity is (a) performing banking or quasi-banking functions, or (b) engaged in other types of financial intermediation shall be decided by the Monetary Board subject to judicial review. For the purpose of resolving such issue; the Monetary Board may, through appropriate supervising department of the Central Bank, examine, inspect or investigate the books and records of such person or entity. The department head and the examiners of said appropriate supervising department are hereby authorized to administer oaths to any such person or director, officer or employee of any

> such entity and to compel the presentation or production of all books, documents, papers or records necessary in their judgment to ascertain the facts relative to the true functions and operations of such person or entity. Failure or refusal to comply with the required presentation or production of such books, documents, papers or records shall subject the persons responsible therefor to the penal sanctions provided under Section 34 of R.A. No. 265, as amended. Persons or entities found by the Monetary Board to be performing banking or quasi-banking functions without the required prior authorization of the Monetary Board may, in addition to the proceedings provided under Section 34 of Republic Act No. 265, as amended, be subject to the imposition of fine of not in excess of ₱500 per day reckoned from the date the unauthorized banking or quasi-banking functions were performed and may be referred to the Securities and Exchange Commission for the revocation of its license to do business.

The record is however bereft of any indication or finding by the Monetary Board that petitioner is a non-banking financial intermediary.

The Court is also not convinced that petitioner's primary purpose as stated in its Articles of Incorporation is sufficient to prove that petitioner is performing the functions of a financial intermediary. Standing alone, such primary purpose is inadequate to justify the conclusion that petitioner is a non-bank financial institution or intermediary or engaged in such activities.

Since respondents utterly failed to establish by convincing and credible evidence that petitioner is a non-bank financial institution/intermediary, or is engaged in such activities, and given that the subject SMC shares of stock have been declared owned by the government, the 0.55% local business tax amounting to ₱1,215,272.00 collected from petitioner for the first and second quarters of 2011 on the dividends arising from its SMC preferred shares and interests on money market placements, is erroneous and/or illegal.

However, for purposes of refund/tax credit of any erroneously levied and collected local tax, fee, or charge, certain conditions under Section 196[13] of the LGC, must first be satisfied, to wit:

1. a written claim for refund or tax credit filed by the taxpayer with the local treasurer; and

2. the court proceeding for refund filed within two (2) years from the date of the payment of the tax, fee, or charge or from the date the taxpayer is entitled to a refund or credit.[14]

Undoubtedly, petitioner was able to fulfill the foregoing requirements. The claim for refund for the local business tax paid under protest for the first and second quarters of 2011 was filed with respondent City Treasurer on September 13, 2012.[15]

As to the judicial claim, evidence show that payments under protest was made by petitioner on January 18, 2011[16] and on April 25, 2011[17]. Petitioner, therefore, had until January 18, 2013 and April 25, 2013, within which to seek judicial remedy. Hence, petitioner's claim for refund was seasonably filed with the RTC on January 17, 2013.[18]

In fine, petitioner is entitled to the refund/tax credit prayed for pursuant to Section 196 of the LGC.

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[13] SEC. 196. *Claim for Refund of Tax Credit.* — No case or proceeding shall be maintained in any court for the recovery of any tax, fee, or charge erroneously or illegally collected until a written claim for refund or credit has been filed with the local treasurer. No case or proceeding shall be entertained in any court after the expiration of two (2) years from the date of the payment of such tax, fee, or charge, or from the date the taxpayer is entitled to a refund or credit.

[14] *China Banking Corporation v. City Treasurer of Manila*, C.T.A. EB No. 182 (RTC Civil Case No. 04-108990), July 27, 2006.

[15] Annex "P-5", Petition for Review, docket, pp. 45-54; Annex "B", RTC Records, pp. 22-31.

[16] Annex "P-3", Petition for Review, docket, p. 43; Annex "A", RTC Records, p. 20.

[17] Annex "P-4", Petition for Review, docket, p. 44; Annex "A-1", RTC Records, p. 21.

[18] Annex "P-6", Petition for Review, docket, pp. 55-71; RTC Records, pp. 3-19.

WHEREFORE, the Petition for Review dated November 3, 2015 filed by Rock Steel Resources, Inc. is **GRANTED**. Accordingly, the assailed Decision dated June 22, 2015 and the Order dated September 11, 2015 of the Regional Trial Court, Branch 16 of Davao City in Civil Case No. 34,855-13 are **REVERSED** and **SET ASIDE**. Respondents are **ORDERED TO REFUND OR CREDIT** in favor of petitioner the amount of ₱1,215,272.00, representing the 0.55% local business tax it paid under protest for the first and second quarters of 2011.

SO ORDERED.

ESPERANZA R. FABON-VICTORINO
Associate Justice

We concur:

LOVELL R. BAUTISTA
Associate Justice

Ma. Belen M. L.
MA. BELEN M. RINGPIS-LIBAN
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.

LOVELL R. BAUTISTA
Associate Justice
Chairperson

CERTIFICATION

Pursuant to Section 13 of Article VIII 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's Division.

ROMAN G. DEL ROSARIO
Presiding Justice