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REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

TRUSTWORTHY PAWNSHOP, INC.,
Petitioner,

- versus - C.T.A. CASE NO. 6236

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:

DEC 06 2001

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DECISION

This is an appeal arising from an assessment issued by the Respondent against the Petitioner involving the latter's alleged liability for Value Added Tax in the amount of P8,859,791.27.

The facts are briefly summarized as follows:

Petitioner is a corporation duly organized and existing under and by virtue of the laws of the Philippines.

The controversy arose when Petitioner received Assessment Notice No. 81-VAT-13-97-2000-6-122 on July 4, 2000 from the Chief of the Assessment Division of Revenue Region No. 13, Cebu City.

Believing that the assessment has no basis in fact and in law, Petitioner filed its protest against the assessment on July 14, 2000 pursuant to Section 228 of the National Internal Revenue Code (Annex B of the Petition for Review, page 13, CTA records).

Unable to obtain an affirmative response from the Respondent, Petitioner elevated its grievance to this Court on February 8, 2001 via Petition for Review.

Petitioner asseverates that Section 102(a) of the NIRC, which serves as Respondent's basis in issuing the assailed assessment notice, does not state that pawnshop businesses are subject to VAT. And that since pawnshop business is not included among those expressly enumerated in the said section, thus, there is no legal basis to subject or assess it for deficiency Value Added Tax.

Upon the other hand, Respondent defends the assessment and advanced the following by way of Special and Affirmative Defenses, to wit:

> "4. Petitioner, as a pawnshop operator, performs services for others for a fee, remuneration or consideration. Its services consist of lending money at interest on the security of personal property, and the interest is the fee, remuneration or consideration for such services. Hence, it is engaged in the sale of services subject to value-added tax (VAT) under Section 102(a) of the Tax Code, as amended by R.A. 7716.
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> 5. Under Section 102(a) of the Tax Code, as amended by R.A. 7716, the VAT is equivalent to 10% of the gross receipts derived from the sale or exchange of services.
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> 6. Interest on pledge loans and past due loans and liquidated damages are part of petitioner's gross receipts subject to VAT.
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> 7. The assessment was issued in accordance with law and regulations.
>
> 8. All presumptions are in favor of the correctness of tax assessments."

Posed for Our resolution now are the following issues:

1. Whether or not the Pawnshop business is subject to Value Added Tax under Section 102 (a) of the Tax Code.

2. Whether interest income is income from service or from forbearance of money.

3. Whether liquidated damages are income from services or a simple item of indemnification.

4. Whether pawnshop business is similar or akin to the Lending Investor business.

5. Whether respondent is legally empowered to impose and charge Value Added Tax on the petitioner for the proceeds of the auction sale of pawned item.

6. Whether pawn ticket is subject to documentary stamp tax.

7. Whether the rate to compute VAT should be Base multiplied by 10% or 1/11.

In its Memorandum, Petitioner reiterates its stance *a quo* and argues that nowhere is it provided in Section 102(a) of the Tax Code that a pawnshop business is subject to Value Added Tax. According to Petitioner, what is provided in the said Section is that lending investors, that used to be subject to the 5% percentage tax, are already subject to VAT under Section 102(a).

Traversing Petitioner's arguments, Respondent posits the view that the enumeration of persons performing services for a fee in Section 102(a) of the Tax Code is merely intended to give examples of businesses subject to VAT on sale or exchange of services, hence, not exclusive. Respondent further submits that the legislative intent is not to limit the application of Section 102(a) to those enumerated therein because the law speaks of "all kinds of services". Another point asserted by the Respondent is that unless the sale or exchange of services is expressly mentioned in Section 103 of the Tax Code as exempt from VAT, such sale or exchange of services is subject to VAT under Section 102(a).

To recapitulate and to arrest the similar nagging problem in the future, it must be stressed anew that pawnshops are not in the same class as lending investors.

Seemingly, the vortex of the controversy lies on the principal activity of pawnshops. To this the following provisions of law are pertinent, thus:

"**Sec. 157. Words and Phrases defined**. – x x x

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

Sec. 161. Fixed Taxes. – x x x

(3) Other fixed taxes. – x x x

(dd) Lending investors –

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

x x x x x x x x x

Sec. 175. Percentage tax on dealers in securities, lending investors. – Dealers in securities shall pay a tax equivalent to six (6%) per cent of their gross income. Lending investors shall pay a tax equivalent to five (5%) per cent of their gross income. (Formerly Section 116.)

Presidential Decree 114 (Pawnshop Regulation Act)

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

> "Pawnshop" shall refer to a person or entity engaged in the business of lending money on personal property delivered as security for loans and shall be synonymous and may be used interchangeably, with pawnbroker or pawnbrokerage.
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> x x x x x x x x x
>
> **Sec. 10. Rates of interest.** – No pawnshop shall directly or indirectly stipulate, charge, demand, take or receive any higher rate or greater sum or value for any loan or forbearance than the rate allowed by the Usury Law for such transactions. x x x"

From the above, it may be inferred that Respondent's ground for the issuance of the assessment notice is meritorious that pawnshops may be in the same class as lending investors since its principal activity is lending money at interest.

Thoroughly analyzing relevant historical background of cases of this nature, Respondent's assertion hinges mainly on RMO 15-91 and RMC 43-91, which We quote hereunder, thus:

RMO No. 15-91, March 11, 1991

> "A restudy of P.D. 114 shows that the principal activity of pawnshops is lending money at interest and incidentally accepting a pawn of personal properties delivered by the pawner to the pawnee as security for the loan. Clearly, this makes pawnshop business akin to lending investor's business activity which is broad enough to encompass the business of lending money at interest by any person whether natural or juridical. Such being the case, pawnshops shall be subject to the 5% lending investor's tax based on their gross income pursuant to Section 116 of the Tax Code, as amended."

RMC No. 43-91, May 27, 1991

> "This Circular subjects to the 5% lending investor's tax the gross income of pawnshops pursuant to Section 116 of the Tax Code, and it thus revokes BIR Ruling Nos. 6-90, and VAT Ruling Nos. 22-90 and 67-90. In order to have a uniform cut-off date, avoid unfairness on the part of

taxpayers if they are required to pay the tax on past transactions, and so as to give meaning to the express provisions of Section 246 of the Tax Code, pawnshop owners or operators shall become liable to the lending investors tax on their gross income beginning January 1, 1991. Since the deadline for the filing of percentage tax return (BIR Form No. 2529A-O) and the payment of the tax on lending investors covering the first calendar quarter of 1991 has already lapsed taxpayers are given up to June 30, 1991 within which to pay the said tax without penalty. If the tax is paid after June 30, 1991, the corresponding penalties shall be assessed and computed from April 21, 1991.

Since pawnshops are considered as lending investors effective January 1, 1991, they also become subject to documentary stamp taxes prescribed in title VII of the Tax Code. BIR Ruling No. 325-88 dated July 13, 1988 is hereby revoked."

Be that as it may, We do not subscribe to the Respondent's view that pawnshops are in the same class as lending investors, accordingly, this Court strikes down the assessment.

The issue in this case is not novel. In **Trustworthy Pawnshop, Inc. vs. Collector of Internal Revenue, CTA Case No. 5691, March 7, 2000,** and in other similar cases, this Court had the occasion to rule in this wise:

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

Further analyzing said Section 161, *supra*, it appears that lending investors were imposed a graduated type of fixed taxes depending on the class of the city or municipality involved while pawnshops were differently levied a flat amount of tax. This particular observation bolster Our position that pawnshops are not similarly situated as lending investors. Congress would not have intended otherwise, because the act of segregating and imposing upon them unequal amount of taxes would transgress the

> fundamental rule on taxation on uniformity or equality enshrined under par. 1, Section 28 of Article VI of our Constitution. The rule requires that all subject or objects of taxation, similarly situated, are to be treated alike or put on equal footing both in privileges and liabilities (**Juan Luna Subdivision vs. Sarmiento, 91 Phil. 371**). It has also been interpreted to mean that all taxable articles or kinds of property of the same class shall be taxed at the same rate (**City of Baguio vs. de Leon, 25 SCRA 938**). Verily, Congress is presumed to have acted in full knowledge of this particular constitutional limitation when it classified pawnshops apart from lending investors."

In the case of **CIR vs. Hon. Andres Reyes, Jr. et. al., CA-G.R. No. 28824, December 23, 1993,** the Court of Appeals made a pronouncement striking down RMO 15-91, the memorandum order which declared pawnshops akin to lending investors, as unconstitutional the power to tax being vested solely with Congress. And We quote, thus:

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

As regards the jointly stipulated issue of whether or not the pawn ticket is subject to documentary stamp tax, the aforequoted Court of Appeals decision in the Andres Reyes case had this to say:

> "Likewise, pawnshop ticket is not subject to documentary stamp tax. The pawn ticket is a pawn broker's receipt for a pawn. It is neither a security nor a printed evidence of indebtedness (Section 3, P.D. 114 or

Pawnshop Regulatory Act). Consequently, it is not subject to documentary stamp tax imposed by Section 195 of the Tax Code"

Prescinding from the above, this Court finds, as amply supported by jurisprudential precepts, that the assessment notice issued by the Respondent lacks legal basis. Accordingly, other issues raised are deemed moot and academic.

WHEREFORE, in view of all the foregoing, the instant Petition for Review is hereby **GRANTED.** Accordingly, Assessment Notice No. 81-VAT-13-97-2000-6-22 is hereby **CANCELLED** and **SET ASIDE.**

SO ORDERED.

AMANCIO Q. SAGA
Associate Judge

WE CONCUR:

ERNESTO D. ACOSTA
Presiding Judge

(Dissenting)
JUANITO C. CASTAÑEDA, JR.
Associate Judge

CERTIFICATION

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

ERNESTO D. ACOSTA
Presiding Judge

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