

REPUBLIC OF THE PHILIPPINES
Court of Tax Appeals
QUEZON CITY

EN BANC

COMMISSIONER OF INTERNAL
REVENUE,

Petitioner,

**C.T.A. EB NO. 507
(C.T.A. CASE NO. 7130)**

Present:

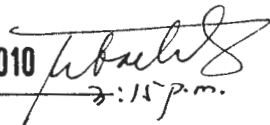
-versus-

ACOSTA, Presiding Justice,
CASTAÑEDA, JR.,
BAUTISTA,
UY,
CASANOVA, and
PALANCA-ENRIQUEZ,
FABON-VICTORINO,
MINDARO-GRULLA, and
COTANGCO-MANALASTAS, JJ.

PHILIPPINE NATIONAL BANK,
Respondent.

Promulgated:

FEB 10 2010


2:15 p.m.

X ----- X

DECISION

PALANCA-ENRIQUEZ, J.:

THE CASE

This is a Petition for Review filed by the Commissioner of Internal Revenue under *Section 2, Rule 4 of the 2005 Revised Rules of the Court of Tax Appeals, as amended*, in relation to *Rule 43 of the 1997 Rules of*



Civil Procedure, as amended, which seeks to reverse and set aside the Decision dated September 16, 2008 and Resolution dated June 29, 2009 rendered by the Former First Division of this Court in C.T.A. Case No. 7130, entitled "Philippine National Bank vs. Commissioner of Internal Revenue", the respective dispositive portions of which read, as follows:

"WHEREFORE, the instant Petition for Review is hereby **GRANTED**. Accordingly, respondent is hereby **ORDERED TO REFUND** to petitioner the amount of **EIGHT HUNDRED SIXTY-FIVE THOUSAND SEVEN HUNDRED THIRTY PESOS AND 26/100 (P865,730.26)**.

SO ORDERED."

"WHEREFORE, finding no cogent reason to reserve the previous ruling of this Court, the Motion for Reconsideration is hereby **DENIED** for lack of merit.

SO ORDERED."

THE PARTIES

Petitioner (hereafter petitioner CIR) is the duly appointed Commissioner of Internal Revenue, with the authority, among others, to decide, approve and grant tax credit and/or refund, and holds office at the 5th Floor, BIR National Office Building, BIR Road, Diliman, Quezon City.



Respondent Philippine National Bank (hereafter “respondent PNB”), on the other hand, is a domestic corporation organized and existing under the laws of the Republic of the Philippines, with principal business address at the PNB Financial Center, President Diosdado Macapagal Blvd., Pasay City.

THE FACTS

The antecedent facts, as summarized by the Former First Division of this Court, are hereunder adopted, to wit:

“Guadalupe Realty Corporation (GRC) had an original loans payable to petitioner (now respondent) in the amount of P68 million, which went up to P83 million due to dollar component. In the middle part of 1997, GRC failed to continue its loan payments due to the economic crisis. Thus, on January 6, 2003, petitioner (now respondent) and GRC entered into a *Dacion En Pago* Agreement, where GRC settled its outstanding obligation of P86,573,025.00 by transferring to petitioner properties mortgaged to it. The properties subject of the *Dacion En Pago* consisted of three (3) parcels of land with improvements and eight (8) condominium units described as follows:

	Unit	Area
Transfer Certificate of Title No. 76036		667 sqm
Transfer Certificate of Title No. 76041		662 sqm
Transfer Certificate of Title No. 76039		653 sqm
Condominium Certificate of Title No. C-386	No. 206	221.70 sqm
Condominium Certificate of Title No. C-388	No. 302	187.85 sqm
Condominium Certificate of Title No. C-397	No. 405	187.85 sqm
Condominium Certificate of Title No. C-400	No. 502	187.85 sqm



Condominium Certificate of Title No. C-408	No. 604	221.70 sqm
Condominium Certificate of Title No. C-412	No. PH2	187.85 sqm
Condominium Certificate of Title No. C-413	No. PH3	221.70 sqm
Condominium Certificate of Title No. C-1640	No. PH1	654.91 sqm

Likewise, GRC and petitioner (now respondent) stipulated that taxes, fees, and expenses to be incurred in connection with the transaction such as, but not limited to, capital gains tax, documentary stamp tax, transfer tax, registration fees, and other expenses shall be paid by petitioner (now respondent).

In compliance with the Agreement, petitioner (now respondent) sought the assistance of Revenue District Office No. 82 (RDO No. 82) for the computation of the corresponding taxes relative to the transaction. Using the outstanding obligation of GRC to petitioner (now respondent) in the amount of P86,573,025.67 as tax base, RDO No. 82 computed petitioner's (now respondent) capital gains tax at P5,194,381.54 and documentary stamp tax at P1,298,610.00.

On January 24, 2003, petitioner (now respondent) filed its Capital Gains Tax Return (CGTR) and Documentary Stamp Tax Return (DSTR); and paid the corresponding taxes. Having settled its tax dues, petitioner (now respondent) was issued a Certificate Authorizing Registration by the Bureau of Internal Revenue (BIR) on July 28, 2003.

Sometime in 2004, petitioner (now respondent) received a letter from the lawyer of GRC informing the former of an assessment against GRC for Value-added Tax (VAT). The letter further reminded petitioner (now respondent) to comply with its obligation to pay all taxes arising from the *Dacion En Pago* Agreement. In response to



the letter, petitioner (now respondent) settled the VAT deficiency of P7,870,275.06 on January 21, 2003.

In the process of settling the VAT deficiency, petitioner (now respondent) reviewed the computation sheet of its capital gains and documentary stamp tax liabilities that was provided by RDO No. 82. Petitioner (now respondent) realized that the BIR, based on the latter's computation, made an improper classification of the properties subject of the *Dacion En Pago* Agreement as capital assets, instead of ordinary assets as recognized in the books of GRC and based on the nature of its use. Petitioner (now respondent) argued that as an ordinary assets, it is only required to withhold five percent (5%) creditable withholding tax based on the consideration of the *Dacion* or fair market value of the property, whichever is higher. Clearly, petitioner (now respondent) erroneously filed a CGTR and paid six percent (6%) withholding tax rate. At the rate of 5% withholding tax, petitioner (now respondent) should have paid only P4,328,651.28 not P5,194,381.54. This resulted in an overpayment of P865,730.26.

Hence, on January 19, 2005, petitioner (now respondent) filed with the BIR a claim for tax refund, representing the alleged excess payment of P865,730.26.

On January 21, 2005, petitioner (now respondent) filed this *Petition for Review* inasmuch as the statutory period of two years mandated by Sections 204(c) and 229 of the National Internal Revenue Code (NIRC) of 1997 for tax refund was due to prescribe on January 23, 2005."

On September 16, 2008, the Former First Division rendered the assailed Decision granting the Petition for Review.



On October 7, 2008, the CIR filed a "Motion for Reconsideration" of said Decision, which was denied for lack of merit by the Former First Division in a Resolution dated June 29, 2009.

Hence, the instant Petition for Review, raising the sole:

ISSUE

WHETHER OR NOT THE HONORABLE COURT
ERRED IN GRANTING RESPONDENT'S CLAIM FOR
REFUND IN THE AMOUNT OF P865,730.26
REPRESENTING ERRONEOUSLY PAID
WITHHOLDING TAXES.

Without necessarily giving due course to the Petition for Review, on August 6, 2009, we ordered respondent PNB to file its comment, not a motion to dismiss, within ten (10) days from notice.

On September 4, 2009, upon motion, respondent PNB was granted a non-extendible period of fifteen (15) days from September 01, 2009 or until September 16, 2009 to file its comment.

On September 16, 2009, respondent PNB filed its "Comment to Petition for Review." Hence, the Petition is now deemed submitted for decision.

gbl

Petitioner CIR's Arguments

Petitioner CIR contends that respondent PNB is not entitled to a claim for refund of allegedly excess taxes paid amounting to P865,730.26; that the real properties subject of the *Dacion En Pago* agreement are capital assets and not ordinary assets for said properties are not primarily held for sale by respondent PNB, the taxpayer herein; moreover, the acquisition or sale of real property by respondent PNB cannot be considered as one in the ordinary course of business for the reason that it is contrary for banks to venture into real estate business, pursuant to *Sections 51 and 52 of RA No. 8791*, otherwise known as the General Banking Act of 2000.

Respondent PNB's Counter-Arguments

Respondent PNB counters that the real properties subject of the *Dacion En Pago* agreement are ordinary assets of an entity, the Guadalupe Realty Corporation ("GRC"), habitually engaged in real estate business; and by law, it is the GRC who is the taxpayer, and not respondent PNB.



THE COURT EN BANC'S RULING

The petition has no merit.

In this regard, *Section 39 (A) (1) of the NIRC of 1997, as amended*, provides:

“SEC. 39. Capital Gains and Losses. -

(A) Definitions. - As used in this Title –

(1) Capital Assets. - the term 'capital assets' means property held by the taxpayer (whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, or property used in the trade or business, of a character which is subject to the allowance for depreciation provided in Subsection (F) of Section 34; or real property used in trade or business of the taxpayer.”

Corollary thereto, *Section 3 of Revenue Regulations No. 7-*

2003 provides:

“SEC. 3. **Guidelines in Determining Whether a Particular Real Property is a Capital Asset or Ordinary Asset.** -

a. Taxpayers engaged in the real estate business. — Real property shall be classified with respect to taxpayers engaged in the real estate business as follows:



XXX

XXX

2. Real Estate Developer. — All real properties acquired by the real estate developer, whether developed or undeveloped as of the time of acquisition, and all real properties which are field by the real estate developer primarily for sale or for lease to customers in the ordinary course of his trade or business or which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year and all real properties used in the trade or business, whether in the form of land, building, or other improvements, shall be considered as ordinary assets.

XXX

XXX

4. Taxpayers habitually engaged in the real estate business. — *All real properties acquired in the course of trade or business by a taxpayer habitually engaged in the sale of real estate shall be considered as ordinary assets.* Registration with the HLURB or HUDCC as a real estate dealer or developer shall be sufficient for a taxpayer to be considered as habitually engaged in the sale of real estate. If the taxpayer is not registered with the HLURB or HUDCC as a real estate dealer or developer, he/it may nevertheless be deemed to be engaged in the real estate business through the establishment of substantial relevant evidence (such as consummation during the preceding year of at least six (6) taxable real estate sale transactions, regardless of amount; registration as habitually engaged in real estate business with the Local Government Unit or the Bureau of Internal Revenue, etc.).

A property purchased for future use in the business, even though this purpose is later thwarted by circumstances beyond the taxpayer's control, does not lose its character as an ordinary asset. Nor does a mere discontinuance of the



active use of the property change its character previously established as a business property.”

Pursuant to the above provision, all real properties acquired in the ordinary course of trade or business by a taxpayer habitually engaged in the sale of real estate shall be considered as ordinary assets. The aforequoted *Section 39 of the NIRC of 1997, as amended*, enumerates what are considered as ordinary assets, namely:

- 1) stock in trade or inventoriable items;
- 2) property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business;
- 3) property used in the trade or business, of a character which is subject to the allowance for depreciation provided in *subsection (F) of Section 34*; and
- 4) real property used in trade or business of the taxpayer.

After a careful examination of the evidence on record, particularly the HLURB Certificate of Registration (*Exhibit “H”*), License to Sell (*Exhibit I”*), GRC’s Articles of Incorporation (*Exhibit “M”*) and Mayor’s Permit (*Exhibit “P”*), the Court finds that GRC is one engaged in the business of selling real estate. A perusal of GRC’s Inventory of



Properties (*Exhibit O-1*) clearly shows that the inventory is a list of properties that are normally held for sale in the ordinary course of GRC's realty business. Petitioner's witness, Mr. Luis Cañete, categorically declared that the properties subject of the *Dacion En Pago* Agreement are part of the list of the properties that were sold by GRC (*tsn, October 5, 2006, pp. 31-32*).

We, therefore, rule that the real properties subject of the *Dacion En Pago* Agreement are ordinary assets of GRC.

Having determined that the real properties subject of the *Dacion En Pago* Agreement are ordinary assets of GRC, we now address the issue of whether respondent PNB is entitled to its claim for refund.

Petitioner CIR claims that the subject real properties should be considered as capital assets with respect to PNB. Though GRC may be considered as a domestic corporation engaged in the business of sales, purchase and development of real estate property, respondent PNB is not and PNB is the taxpayer herein; that in the case of respondent PNB, the acquisition or sale of real property cannot be considered as one made in the ordinary course of business, being contrary to the provisions of the



General Banking Act of 2000; and to declare that the acquisition of real estate made by respondent PNB falls under the ordinary course of business of banking would in effect and indirectly expand the definition of banking, and would allow banks, blessed with immense purchasing power, to unduly and rampantly roam the open field of real estate.

On the other hand, respondent PNB claims that pursuant to the *Dacion* Agreement between GRC and respondent PNB, it is clear that the owner, seller, and transferor, contemplated by *Revenue Regulations No. 2-98, as amended*, pertains to GRC and not respondent PNB, because it is GRC who is the owner, seller, and transferor of the dacioned assets consisting of 3 parcels of land and 8 condominium units; that it is therefore the qualification of the owner, seller, or transferor, as to whether or not it is an entity habitually engaged in real estate business, which becomes controlling; that the qualification of the buyer or transferee, like respondent PNB, has nothing to do with the computation of payment of capital gains tax or creditable withholding tax relative to the sale or transfer of real properties, contrary to what petitioner CIR would want to portray in his petition before the Court *En Banc*.



We rule for respondent PNB.

While records show that it was GRC which was assessed by the BIR, it is clear in the *Dacion En Pago* Agreement between GRC and respondent PNB that the taxes, fees, and expenses to be incurred in connection with the transaction such as, but not limited to capital gains tax, documentary stamp tax, transfer tax, registration fees, and other expenses shall be paid by PNB (*Exhibit "A-3"*).

Considering that the real properties subject of the *Dacion En Pago* Agreement fall within the definition of those properties primarily sold to customers in the ordinary course of business, it is clear that the payment of the 6% capital gains tax is in excess of the 5% withholding tax prescribed by *Section 2.57.2 of Revenue Regulations (RR) No. 2-98, as amended*, which provides, as follows:

“SEC. 2.57.2. Income Payment subject to creditable withholding tax and rates prescribed thereon.

—

Except as herein otherwise provided, there shall be withheld a creditable income tax at the rates herein specified for each class of payee from the following items of income payments to persons residing in the Philippines:

xxx

xxx



(J) *Gross selling price or total amount of consideration or its equivalent paid to the seller/owner for the sale, exchange or transfer of.* –

Real property, other than capital assets, held by an individual, corporation, estate, trust, trust fund or pension fund and the seller/transferor is habitually engaged in the real estate business in accordance with the following schedule –

Those which are exempt from withholding tax at source as prescribed in sec. 2.57.5 of these regulations	Exempt
With a selling price of P500,000 or less	1.5%
With a selling price of more than P500,000 but not more than P2,000,000	3.0%
With a selling price of more than P2,000,000	5.0%

A seller/transferor must show proof of registration with HLURB or HUDCC to be considered as habitually engaged in the real estate business.”

Pursuant to the *Dacion En Pago* Agreement between GRC and respondent PNB, it is clear that the owner, seller, transferor contemplated by RR No. 2-98, as amended, pertains to GRC and not to respondent PNB, because it is GRC who is the owner, seller, transferor of the real properties subject of the *Dacion En Pago* Agreement, consisting of three (3) parcels of land and eight (8) condominium units. It is, therefore, the nature of the business of the owner, seller, transferor, as to whether or not it is an entity habitually engaged in real estate business, which is controlling.



As aptly ruled by the Former First Division:

“Considering that the properties subject of the *Dacion En Pago* Agreement meet the elements of those primarily sold to customers in the ordinary course of business; the logical conclusion is that the payment of the 6% capital gains tax is in excess of the 5% withholding tax required by RR 2-98.

Anent the fourth issue of whether or not petitioner paid or remitted to the BIR the amount of taxes withheld representing 6% of the selling price, this Court again rules in the affirmative.

In a contract of *Dacion En Pago*, what is deemed as the purchase price is the amount of the debt or mortgage; in this case, the amount of P86,573,025.67. In the case of **Vda. De Jayme, et al. vs. Court of Appeals, et al.**, the High Court said that:

‘Dacion en pago is the delivery and transmission of ownership of a thing by the debtor to the creditor as an accepted equivalent of the performance of the obligation. **It is a special mode of payment where the debtor offers another thing to the creditor who accepts it as equivalent of payment of an outstanding debt. The undertaking really partakes in one sense of the nature of sale, that is, the creditor is really buying the thing or property of the debtor, payment for which is to be charged against the debtor’s debt. As such, the essential elements of a contract of sale, namely, consent, object certain, and cause of consideration must be present. In its modern concept, what actually takes place in dacion en pago is an objective novation of the obligation where the thing offered as an accepted equivalent of the**



performance of an obligation is considered as the object of the contract of sale, while the debt is considered as the purchase price. In any case, comment consent is an essential prerequisite, be it sale or novation, to have the effect of totally extinguishing the debt or obligation.' (*Emphasis supplied*)

Petitioner submitted to the Court its CGTR, together with the corresponding bank deposit slip proving payment, and its Certificate Authorizing Registration; all showing that 6% of the selling price of P86,573,025.67, or P5,194,381.54 was duly settled by petitioner.

Going now to the sixth and seventh issue pertaining to the right of petitioner to claim for tax refund, the Court also rules in petitioner's favor.

It has been an established rule in taxation that a withholding agent is not an ordinary agent, he is an agent of both the State and the taxpayer. With respect to the collection and/or withholding of the tax, he is the Government's agent. In regard to the filing of the necessary Income Tax Return and the payment of the tax to the Government, he is the agent of the taxpayer. The withholding agent, therefore, is held personally liable for the tax he is duty bound to withhold. The authority of filing the necessary income tax and payment thereof necessarily implies the authority of the withholding agent to file a claim for refund and to bring an action in recovery of that claim.

Petitioner was able to sufficiently establish its personality to file this case and that no double claim for the same excess tax payment was made. Petitioner proved these by presenting a Certification issued by BIR Revenue District No. 82 of Cebu City, stating that GRC did not file any administrative claim for refund worth P865,730.26 relative



to the *Dacion* Agreement. It also showed that no future claim for refund shall be filed by GRC considering that it is already a dissolved corporation beginning March 31, 2003 when GRC sought the cancellation of its registration.

The above discussion has adequately ascertained the fact of erroneous payment of capital gain tax of 6% instead of the withholding tax of 5%. It is thus, unfair for the Government to deny this valid claim of petitioner as it has the duty to act fairly at all times.”

Finding no reversible error, we affirm the Decision dated September 16, 2008 and Resolution dated June 29, 2009 rendered by the Former First Division of this Court.

WHEREFORE, premises considered, the present Petition for Review is hereby **DENIED DUE COURSE**, and, accordingly **DISMISSED** for lack of merit.

SO ORDERED.


OLGA PALANCA-ENRIQUEZ
Associate Justice

WE CONCUR:

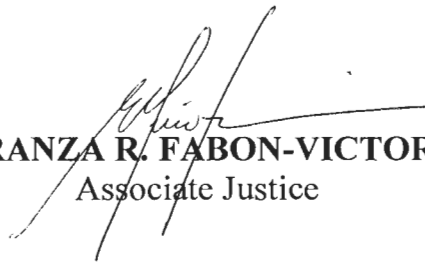

ERNESTO D. ACOSTA
Presiding Justice

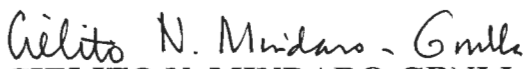

JUANITO C. CASTAÑEDA, JR.
Associate Justice

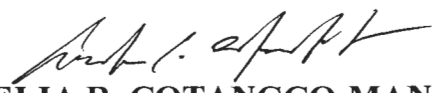

LOVELL R. BAUTISTA
Associate Justice


ERLINDA P. UY
Associate Justice


CAESAR A. CASANOVA
Associate Justice


ESPERANZA R. FABON-VICTORINO
Associate Justice


CIELITO N. MINDARO-GRULLA
Associate Justice


AMELIA R. COTANGCO-MANALASTAS
Associate Justice

CERTIFICATION

Pursuant to Section 13, Article VIII of the Constitution, it is hereby certified that the above Decision has been reached in consultation with the members of the Court *En Banc* before the case was assigned to the writer of the opinion of the Court.


ERNESTO D. ACOSTA
Presiding Justice