REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

FIRST DIVISION

SAN MIGUEL OFFICERS CORPS, INC., *Petitioner,*	CTA AC No. 161 (Civil Case No. 34, 856-13)
-versus-	*Present*: DEL ROSARIO, P.J., UY, and MINDARO-GRULLA, *JJ.*
CITY OF DAVAO and HON. RODRIGO S. RIOLA, in his capacity as the City Treasurer of Davao City, *Respondent.*	Promulgated: OCT 03 2016 ; 3:00 p.m.

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DECISION

MINDARO-GRULLA, J.:

This is a Petition for Review[1] filed by San Miguel Officers Corps Inc., (SMOCI) on November 9, 2015, pursuant to Section 7(a)(3)[2] of Republic Act No. 1125,[3] as amended, in relation to Section 4(a) of Rule 8 of the Revised Rules of the Court of Tax Appeals (RRCTA), seeking to reverse and set aside the Decision[4] dated June 22, 2015 issued by the Regional Trial Court (RTC) Branch 16 of Davao

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[1] CTA Docket, pp. 8-28.

[2] SEC. 7. Jurisdiction. - The CTA shall exercise:

(a) Exclusive appellate jurisdiction to review by appeal, as herein provided:

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(3) Decisions, orders or resolutions of the Regional Trial Courts in local tax cases originally decided or resolved by them in the exercise of their original or appellate jurisdiction;

xxx xxx xxx

[3] An Act Creating the Court of Tax Appeals.

[4] CTA Docket, pp. 32-41.

City in Civil Case No. 34, 856-13 entitled "San Miguel Officers Corps, Inc. vs. City of Davao and Hon. Rodrigo S. Riola, in his official capacity as the City Treasurer of Davao City", dismissing petitioner's claim for refund or credit of local business tax, and the Order[5] dated September 11, 2015, denying petitioner's Motion for Reconsideration.

SMOCI is a domestic corporation existing under and by virtue of Philippine laws, with principal office address at Legaspi Oil Compound, Km. 9.5, Sasa, Davao City.[6]

City of Davao is a local government unit duly created by law; while Rodrigo S. Riola is being sued in his official capacity as City Treasurer of Davao City, both with office address at City Hall Building, San Pedro Street, Davao City.[7]

Since October 2009, SMOCI is the registered owner of fifty three million eight hundred sixty three thousand thirty five (53,863,035) preferred shares of stock in San Miguel Corporation (SMC) after the Supreme Court approved the conversion of SMOCI's fifty three million eight hundred sixty three thousand thirty five (53,863,035) SMC common shares of stock into SMC Preferred shares; and the dividends received by SMOCI from said preferred shares were deposited in a trust account which earned interest from money market placements.

Respondents collected payment from SMOCI local business tax for the first and second quarters of 2011 on the dividends received by SMOCI from its SMC preferred shares and interests on money market placements in the aggregate amount of one million one hundred twenty four thousand and sixty four pesos (₱1,124,064.00).[8]

On September 13, 2012, SMOCI filed with Riola its written administrative claim for refund or credit of erroneously and illegally collected local business tax. Despite the lapse of four (4) months, SMOCI's written claim for

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[5] CTA Docket, p. 42.
[6] Annex P-10, CTA Docket, p. 101.
[7] Petition for Review, CTA Docket, par. 12, p. 11.
[8] Annexes "A" and "A-1," RTC Records.

refund or credit has not been acted upon and resolved by Riola.

Due to the inaction of Riola on SMOCI's claim, the latter filed a Petition for Review[9] on January 17, 2013 before the RTC Branch 16 of Davao City.

The RTC denied the Petition for Review in a Decision[10] promulgated on June 22, 2015, on the ground that SMOCI is a non-bank financial intermediary and is therefore subject to local business tax on its dividends and interest income.

In its Order[11] dated September 11 2015, the RTC denied SMOCI's Motion for Reconsideration.[12]

Thus, SMOCI filed the instant Petition for Review.[13]

Comment[14] was filed by respondents on January 4, 2016 through registered mail. The respective Memoranda[15] for SMOCI and respondents were received by this Court on March 17, 2016 and March 23, 2016, respectively.

SMOCI argues that it is erroneous and illegal for respondents to assess local business tax on its dividends and interest income because it is not a bank or a financial institution pursuant to Section 133(a)[16] of R.A. No. 7160.[17] SMOCI insists that it is a holding company and is prohibited from acting as an investment company or a securities broker and/or dealer as shown in its Amended Articles of

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[9] CTA Docket, pp. 55-70.
[10] *Supra*, note 4.
[11] *Supra*, note 5.
[12] CTA Docket, pp. 72-80.
[13] *Supra*, note 1.
[14] CTA Docket, pp. 151-164.
[15] CTA Docket, pp. 170-195; 200-216.

[16] SEC. 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;

[17] Local Government Code of the Philippines.

Incorporation. SMOCI argues that it is not a bank within the definition/meaning under Section 131 of the LGC nor the definition/meaning under Revenue Regulations No. 9-2004 and Section 4101Q.1[18] of the Manual of Regulations for Non-Bank Financial Institutions.

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[18] **"§ 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 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;
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> b. Use principally the funds received for acquiring various types of debt or equity securities;
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> c. Borrow against, or lend on, or buy or sell debt or equity securities;
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> d. Hold assets consisting principally of debt or equity securities such as promissory notes, bills of exchange, mortgages, stocks, bonds, and commercial papers;
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> 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.

Allegedly, it was neither required by the Securities and Exchange Commission to secure a secondary license nor regulated by the BSP or the Insurance Commission for SMOCI to fall within the ambit of the phrase "banks and other financial institutions" under Section 131(e)[19] of R.A. No. 7160.

SMOCI added that the phrase "gross sales or receipts" does not include interests and dividends as subject to local business tax under Section 131(n) of R.A. No. 7160. In its Opinion dated March 17, 2011, the Bureau of Local Government Finance (BLGF) ruled that any tax imposed on interest or dividends of non-bank and non-financial institutions assumes the nature of income tax, which local government units are expressly prohibited from levying under Section 133(a) of R.A. No. 7160.

It is SMOCI's position that its receipt of dividends and interest income as a consequence of its ownership of SMC shares of stock and money market placements is not a business activity that is subject to local business tax. It is SMOCI's stand that the tax on the dividends on the SMC shares of stocks it holds are considered as income tax which respondents are not allowed to levy under Section 133(a) of R.A. No. 7160.

It likewise alleges that its income partake the nature of public funds; hence, business tax cannot be imposed on the same.

On the other hand, respondents contend that SMOCI is a non-bank financial intermediary based on the latter's Amended Articles of Incorporation. Respondents allege that

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(3) A person or entity performing any of the functions enumerated in Items a to e of this Subsection."

[19] "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;

the stated primary purpose of SMOCI in the said Articles of Incorporation is 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* (BSP); and the statement that the latter shall not act as an investment company or securities broker or dealer is not a conclusive proof of not being a bank or other financial institution. As a result, SMOCI was assessed for local business tax under Section 143(f) of R.A. No. 7160 and Sections 5(b)(3) and 69(f) of Ordinance No. 158-05, Series of 2005, in relation to Section 131(e) of R.A. No. 7160.

According to respondents, although dividends and interest income are not included in the general definition of gross sales/receipts under Section 131(n) of R.A. No. 7160, it cannot defeat a specific and clear provision of taxability of dividends and interest income, as provided under Section 143(f) of the same Code. Respondents further claim that even if SMOCI's income partake the nature of public funds pursuant to the ruling in the case of *Cocofed vs. Republic*,[20] the dividends and interest income received by SMOCI are subject to the local business tax under Section 143(f) of R.A. No. 7160.

The crux of the issue is whether SMOCI is a non-bank financial intermediary so that its dividends and interest income are subject to local business tax.

The Court finds that SMOCI cannot be categorized as a non-bank financial intermediary.

Consistent with the Local Government Code, Section 69 (f) of Davao City's Ordinance No. 158-05, Series of 2005, otherwise known as the 2005 Revenue Code of Davao City, is explicit in imposing business tax on banks and financial institutions based on gross receipts derived from interest and dividends, *viz.:*

[20] G.R. Nos. 177857-58, January 24, 2012.

> "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: XXX
>
> > F. <u>On Banks and Other Financial Institutions</u>, 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, insurance premium. All other income and receipts not herein enumerated shall be excluded in the computation of the tax." (Underlining supplied)

In upholding the imposition of local business tax by respondents on SMOCI, the court *a quo* concluded that SMOCI falls within the category of "non-bank financial intermediary."

Non-bank financial intermediaries are defined as "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."[21] The person or entity must perform the aforementioned functions on a regular and recurring basis, and not on an isolated basis.

After a careful examination of the records, it appears that there is no sufficient evidence proving that SMOCI is a financial intermediary or has even engaged in the activities of a financial institution/intermediary.

The Court is not convinced that the stated primary purpose of SMOCI in the Amended Articles of Incorporation is broad enough to catch all the descriptive functions of a

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[21] BIR Revenue Regulations No. 12-2003.

financial intermediary. It is not proper to just assume that SMOCI is engaged as a non-bank financial intermediary based on the said primary purpose.

Parenthetically, there is nothing in SMOCI's Amended Articles of Incorporation that suggests, even remotely, that such entity may perform the functions of a financial intermediary. Rather, the primary purpose for which SMOCI was incorporated is to "direct the operations of other corporations through the ownership of stock therein", and "to do every act and thing covered generally by the denomination 'holding company'", to wit:

> "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."[22]

Moreover, while the Amended Articles of Incorporation is categorical in proscribing SMOCI from acting "as an investment company or a securities broker and/or dealer nor exercise the functions of a trust corporation", its

[22] Annex P-10, CTA Docket, pp. 102-103.

identification as a holding company is consistent with the definition of a holding company provided for in Securities and Exchange Commission, Office of the General Counsel (SEC-OGC) Opinion No. 11-15 dated February 10, 2011,[23] as follows:

> "A holding company has been defined by the Commission in several opinions. A holding company has been aptly defined as "a corporation organized to hold the stock of another or other corporations. Its essential feature is that it holds stock. The term "holding company" is equivalent to a parent corporation, having such an interest in another corporation, or power of control, that it may elect its directors and influence its management. A parent or holding company is one that controls another as a subsidiary or affiliate by the power to elect its management. Affiliates are those concerns that are subject to common control and operated as part of a system."

Being a holding company, it is beyond the reach of local taxation.[24]

It must be stressed that it is the corporation's purpose clause that confers, as well as limits, the powers which a corporation may exercise. The main evidence of the purpose of a corporation is its articles of incorporation considering that such information is required by statute to be stated in the incorporation document.[25]

Also, although the purpose clause in SMOCI's Amended Articles of Incorporation is broad and does allow for the acquisition of shares of stock of other corporations and "to receive, collect and dispose of the interest dividends and

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[23] SEC-OGC Opinion No. 11-15, Applicability of Foreign Ownership Restriction; Holding Companies, cited in *Anglo Ventures Corporation vs. City of Davao and Hon. Rodrigo S. Riola, in his capacity as the City Treasurer of Davao City,* CTA AC No. 155, July 12, 2016.
[24] *Michigan Holdings Inc., vs. the City Treasurer of Makati City, Nelia A. Barlis*, CTA EB No. 1093, June 17, 2015.
[25] *Jesus Sacred Heart College vs. Collector of Internal Revenue*, G.R. No. L-6807, May 24, 1954, cited in *Anglo Ventures Corporation, Supra* note 23; *Commissioner of Internal Revenue vs. Court of Appeals,* G.R. No. 124043, October 14, 1998.

income arising from such property", it is clear from a reading of the same that its primary purpose is not to engage in business as a non-bank financial intermediary. The receipt of dividend and interest income is patently incidental. As a holding company, SMOCI, and the other holding companies funded by the coconut levy fund, were created to hold SMC shares of stock,[26] and not to engage in the business of lending or investing money or securities acquired by them or through them, on a regular basis.

Anent respondents' claim that the proviso at end of SMOCI's purpose clause, i.e. "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" -- is intended to conceal or mislead, or exempt SMOCI from obtaining the necessary secondary license, such contention is not supported by evidence. Basic is the rule that he who alleges a fact has the burden of proving it and a mere allegation is not evidence.[27]

In addition, it must be emphasized that 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 is vested in the Monetary Board subject to judicial review.[28]

Moreover, in *Commission of Internal Revenue vs. Hantex Trading Co., Inc.*,[29] the Supreme Court ruled that an assessment must be based on actual facts. Accordingly, the local business tax assessment should be based on actual facts. And since there is no proof that SMOCI can be considered as a non-bank financial intermediary or is engaged in such activities, the local business tax assessment has no factual basis.

In fine, it is clear that respondents' collection of the disputed business tax is erroneous. As respondents received

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[26] *Supra* note 20.
[27] Luxuria Homes Inc., vs. Court of Appeals, G.R. No. 125986, January 28, 1999, cited in *Anglo Ventures, Supra* note 15.
[28] Section 4 of R.A. No. 337, as amended and further amended by P.O. No. 1828
[29] G.R. No. 136975, March 31, 2005, citing *Collector of Internal Revenue vs. Benipayo*, 4 SCRA 182 (1962).

the amount when in fact it is not legally due to the City of Davao, respondents are duty-bound to credit or to refund the same to SMOCI.

WHEREFORE, premises considered, the instant Petition for Review is hereby **GRANTED**. Accordingly, the assailed Decision and Order are hereby **REVERSED**, and the City of Davao is hereby **ORDERED** to **REFUND** or **CREDIT** the amount of **ONE MILLION ONE HUNDRED TWENTY FOUR THOUSAND AND SIXTY FOUR PESOS (₱1,124,064.00)**, representing the erroneously or illegally paid local business tax in favor of San Miguel Officers Corps, Inc.

SO ORDERED.

Cielito N. Mindaro-Grulla
CIELITO N. MINDARO-GRULLA
Associate Justice

WE CONCUR:

ROMAN G. DEL ROSARIO
Presiding Justice

ERLINDA P. UY
Associate Justice

CERTIFICATION

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

ROMAN G. DEL ROSARIO
Presiding Justice