REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

INTERNATIONAL EXCHANGE BANK,
Petitioner,

- versus -

C.T.A. CASE NO. 6225

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:

FEB 19 2002

x - x

DECISION

This case involves a claim for refund of the amounts of P1,125,481.75 and P225,096.35 allegedly representing capital gains tax (CGT) and documentary stamp tax (DST), respectively, paid by Petitioner, as statutory-seller in a foreclosure sale.

Petitioner is a commercial banking corporation duly organized and existing under Philippine laws with principal office at 142 Amorsolo Street, Legaspi Village, Makati City.

The facts as borne out from the records are stated as follows:

Rick Poblete and Sons Agricultural Enterprises, Inc.(Poblete and Sons, for brevity), is a corporation duly organized and existing under and by virtue of the laws of the Republic of the Philippines (Annex "A").

On March 12, 1998, Poblete and Sons obtained a loan from Petitioner and as security for the loan, mortgaged a parcel of land, with improvements thereon, situated at Edison Street, Barangay San Isidro, Makati City and covered by TCT No. S-79365. A Real Estate Mortgage was executed thereon.

On January 12, 1999, for failure by Poblete and Sons to pay its loan, the property mortgaged to Petitioner was foreclosed extrajudicially and an auction sale was conducted in accordance with Act No. 3135, as amended. Being the highest bidder, the subject property was awarded to Petitioner which tendered a bid price of Fifteen Million Six Thousand Four Hundred Twenty Three and 03/100 Pesos (P15,006,423.03).

Petitioner paid the BIR the amounts of P1,125,481.75 on January 26, 1999 and the DST of P225,096.35 on February 2, 1999, representing the CGT and DST, respectively. The Certificate of Sale was registered by Petitioner with the Registry of Deeds of Makati City on February 10, 1999.

As stated in the Joint Stipulation of Facts and Issues, on February 2, 2000, Poblete and Sons assigned its rights over the mortgaged property to Amuson Realty Development Corporation (Amuson, for brevity), a domestic corporation organized and existing under the laws of the Republic of the Philippines. Amuson paid the BIR the sum of P1,650,000.00 as Creditable Withholding Tax (CWT) while Poblete and Sons paid the sum of P330,000.00 as DST on the assignment and/or transfer of rights.

On February 7, 2000 or three (3) days before the expiration of the redemption period, Amuson instituted a complaint for consignation and redemption against Petitioner docketed as Civil Case No. 00-198 with Branch 139, Regional Trial Court of Makati City. In its Decision dated May 24, 2000 based on the Compromise Agreement executed between the parties, the Court allowed Amuson to redeem the property after payment of the redemption price.

Amuson paid Petitioner the amount of P17,150,000.00 but which did not include the amount corresponding to the CGT and DST paid on the foreclosure sale. Pursuant to the Court Order dated May 24, 2000, a Certificate of Redemption was executed by Petitioner in favor of Amuson.

Amuson and Petitioner have allegedly agreed that the latter shall be the one to file an application for tax refund of the CGT and DST.

On July 18, 2000, Petitioner filed an administrative claim with the Appellate Division of the BIR corresponding to the CGT and DST paid on the foreclosed property.

Unable to obtain a response from the Respondent, and in order to toll the running of the two (2) year prescriptive period, Petitioner filed its judicial claim with this Court on January 16, 2001.

Petitioner maintains that no gain or income was derived from the foreclosure sale since the property was not sold nor transferred for a consideration but was redeemed by the owner, through its assignee. It further averred that in a foreclosure sale, the transfer of ownership ensues only upon expiration of the redemption period provided under Act No. 3135, as amended, and the foreclosed property was redeemed before the lapse of the prescribed period.

Respondent, on the other hand, raised the following affirmative defenses in his Answer filed on March 2, 2001, to wit:

> "11. The petition in the instant case states no cause of action. Petitioner is not entitled to its claim for tax refund, because it was actually the withholding agent with respect to taxes due to be withheld on capital gains realized from the sale of land. As withholding agent, petitioner was mandated to deduct, withhold, and pay taxes under Sections 57 and 58 of the Tax Code.
>
> 12. Tax refunds are in the nature of tax exemptions. As such, they are regarded as in derogation of sovereign authority and to be construed *strictissimi juris* against the person or entity claiming the exemption. Based on this the instant case should have been dismissed outright because

its allegations are insufficient to show that petitioner is entitled to claim tax refund."

On June 20, 2001, Petitioner filed a "Motion for Summary Judgment" considering that the facts upon which the instant petition is premised are undisputed, and that only legal issues are to be resolved. Respondent filed his Comment thereto on July 12, 2001. On July 19, 2001, the Court granted Petitioner's "Motion for Summary Judgment."

The sole issue, as jointly stipulated by the parties is: Whether or not Petitioner (iBank) is entitled to a refund of the capital gains tax on gain and documentary stamp tax it paid on the sale of a foreclosed property despite redemption thereof within the statutory period of one year.

Petitioner basically anchored its claim on the provisions of Revenue Regulations (RR) No. 4-99, particularly Sections 3 and 4 thereof, to wit:

> "**SEC. 3.** *CAPITAL GAINS TAX.* -
>
> (1) In case the mortgagor exercises his right of redemption within one year from the issuance of the certificate of sale, no capital gains tax shall be imposed because no capital gains has been derived by the mortgagor and no sale or transfer of real property was realized. xxx"
>
> xxx xxx xxx
>
> "**SEC. 4.** *DOCUMENTARY STAMP TAX.* -
>
> (1) In case the mortgagor exercises his right of redemption, the transaction shall only be subject to the P15.00 documentary stamp tax imposed under Sec. 188 of the Tax Code of 1997 because no land or realty was sold or transferred for a consideration. xxx "

The aforequoted regulation governs the payment of capital gains tax and documentary stamp tax on extrajudicial foreclosure sale of capital assets initiated by banks, finance and insurance companies. RR No. 4-99 dated March 9, 1999 was issued by the Secretary of Finance in order to prevent the inequity that will arise if the capital gains tax is collected before the expiration of the redemption period.

Section 6 of Act No. 3135, as amended, provides:

> "**Section 6.** – In all cases in which an extrajudicial sale is made under the special power herein before referred to, the debtor, his successors in interest or any person having a lien on the property subsequent to the deed of mortgage or trust under which the property is sold, may redeem the same within the term of one year from and after the date of sale"

It is well-settled that in a foreclosure sale, transfer of ownership ensues only upon expiration of the redemption period as aforecited. Verily, the debtor/mortgagor is given the opportunity to re-acquire ownership of his foreclosed property within one-year reckoned from the date of registration of the Certificate of Sale as provided under Section 33 of Rule 39 of the 1997 Rules of Civil Procedure, which reads as follows:

> **"RULE 39**
>
> **Section 33.** – If no redemption be made within one (1) year from the date of registration of the certificate of sale, the purchaser is entitled to a conveyance or possession of the property xxx. "

It bears stressing that what is being subjected to the capital gains tax is not the transfer of ownership *per se* but the profit or gain that was presumed to have been realized by the seller/mortgagor arising from the transfer. The concept of income implies gain, profit or flow of wealth **(Madrigal vs. Rafferty, 38 PHIL 414).** Hence, it is necessary that the debtor/mortgagor should have profited, materially or otherwise, from the foreclosure sale where the properties were redeemed within the specified period under Act No. 3135, as amended. Since the debtor-mortgagor did not earn any income from the sale of the foreclosed property, then it follows that it is not liable to pay the CGT.

The inequity of collecting the capital gains tax before the expiration of the redemption period was acknowledged by the Respondent in BIR Ruling No. 006-92 which provided for the solution of refunding the same in case the right of redemption is exercised, to wit:

> "In foreclosure sales of mortgaged properties, the creditor-bank is the statutory seller, representing the owner-mortgagor of the property, so that said bank becomes liable for the capital gains tax due on such foreclosure sale based on the bid price in the auction sale. However, said bank could get reimbursement or recovery of the capital gains tax payment, if the right of redemption is exercised by the debtor-mortgagor or when the property is sold to any party whatsoever."

In view of the provisions of RR No. 4-99, particularly Section 3, this Court has ruled in a number of cases that since no capital gains have been derived by the debtors-mortgagors in the foreclosure sale, the imposition of the corresponding capital gains tax is not warranted, hence, the claims for refund in these cases were granted. The Court has ruled in this wise:

> "It bears stressing that it is not the transfer of ownership per se that subjects the sale to the 5% capital gains tax but the profit or gain that was presumed to have been realized by the seller/mortgagor by means of said transfer as can be clearly seen from the provisions of Section 21(e) of the Tax Code (supra). Let us not forget that the capital gains tax is an income tax defined as a tax on a person's income, wages, salary commissions, emoluments, profits and the like (*Black's Law Dictionary, 6th Edition*). The concept of income implies gain, profit or flow of wealth (*Madrigal vs. Rafferty, 38 PHIL 414*). The question that should be asked at this point is: Did the Petitioners profit or gain anything from the foreclosure sale where the properties were redeemed within the specified redemption period? The answer is obvious. Petitioner did not earn any income from the sale of these foreclosed properties, hence they should not be made liable to pay the capital gains tax.
>
> xxx xxx xxx
>
> As said RR 4-99 states, no capital gains having been derived by the mortgagor (Petitioners, in the instant case), then no capital gains tax shall

> be imposed. It will be unjust to deprive the Petitioners their right to refund the capital gains tax which they already paid on the foreclosure sale of their properties when the facts show that they redeemed these properties within the period specified by the law." (*Spouses Arturo Soriano and Virginia T. Soriano vs. Hon. Liwayway Vinzons-Chato as Commissioner of Internal Revenue, CTA Case No. 5563, promulgated on June 22,1999, with Entry of Judgment dated August 13, 1999*)"

Firstly, the transfer of ownership of real property whether treated as capital or ordinary asset ensues only upon expiration of the redemption period provided under Section 6 of Act No. 3135, as amended.

Secondly, regardless of whether the property foreclosed is treated as a capital asset or ordinary asset, the fact remains that in case redemption is effected within the period provided under Section 6 of Act No. 3135, as amended, the debtor-mortgagor did not earn any income from the foreclosure sale.

On the issue of documentary stamp tax imposed on the foreclosure sale. We agree with the Petitioner that the transaction is subject only to P15.00 documentary stamp tax pursuant to Section 4 of RR 4-99.

The need of the Government to raise revenues to defray its expenses and to continuously serve its people, should not be done at the expense of justice and equity. Thus, in **Roxas vs. Court of Appeals, 127 SCRA 276**, the Supreme Court held:

> "The power of taxation is sometimes called the power to destroy. Therefore, it should be exercised with caution to minimize injury upon the proprietary rights of the taxpayer. It must be exercised fairly, equally and uniformly, lest the tax collector kills the "hen that lays the golden egg." And in order to maintain the general public's trust and confidence in the government, this power must be used justly and not treacherously."

Considering that the claimed CGT and DST have been paid by Petitioner which is not disputed by the Respondent, the claim for refund should be granted.

WHEREFORE, in the light of all the foregoing, the instant Petition for Review is **GRANTED**. Respondent is hereby **ORDERED** to **REFUND** in favor of Petitioner the amounts of P1,125,481.75 and P225,096.35 representing capital gains tax and documentary stamp tax, respectively, paid on the foreclosure sale of the subject property.

SO ORDERED.

AMANCIO Q. SAGA
Associate Judge

WE CONCUR:

ERNESTO D. ACOSTA
Presiding Judge

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