Republic of the Philippines
COURT OF TAX APPEALS
Quezon City

EN BANC

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

- versus -

AQUAFRESH SEAFOODS, INC.,
Respondent.

CTA-E.B. NO. 77
(C.T.A. Case No. 6409)

Present:

Acosta, *P.J.,*
Castañeda, Jr.,
Bautista,
Uy,
Casanova, and
Palanca-Enriquez, *JJ.*

Promulgated:

NOV 0 9 2005 [signature]

x - x

DECISION

UY, *J.*:

This is a Petition for Review filed before the Court of Tax Appeals *En Banc* under Section 11 of Republic Act No. 9282, assailing the Decision of the First Division of the Court of Tax Appeals promulgated on December 22, 2004 in CTA Case No. 6409 entitled, "Aquafresh Seafoods, Inc. vs. Commissioner of Internal

Revenue and Regional Director, BIR Revenue Regional No. 11-Iloilo City", as well as the Resolution promulgated on April 4, 2005 denying the motion for reconsideration of the said Decision, the respective decretal portions of which read:

> **Decision dated December 22, 2004:**
>
> *"IN VIEW OF THE FOREGOING, respondent's assessments for deficiency capital gains tax and documentary stamp taxes are hereby CANCELLED and SET ASIDE. However, petitioner is ORDERED to PAY the respondent deficiency capital gains and documentary stamp taxes in the sum of P394,197.22, computed as follows:*
>
> | | *CGT* | *DST* |
> |---|---|---|
> | *Basic Deficiency Tax* | *P 211,970.57* | *52,995.00* |
> | *Add: 25% Surcharge* | *52,992.64* | *13,248.75* |
> | *20% Interest* | *50,508.35* | *12,481.91* |
> | *Total Deficiency Taxes Dues* | *P315,471.56* | *P78,725.66* |
>
> *plus 20% delinquency interest computed from October 17, 2000 until fully paid pursuant to Section 249 of the 1997 Tax Code.*
>
> *SO ORDERED."*[1]
>
> **Resolution dated April 4, 2005:**
>
> *"WHEREFORE, finding no cogent reason to disturb the Court's findings and conclusion, respondent's Motion for Reconsideration is hereby DENIED for utter lack of merit.*
>
> *SO ORDERED."*[2]

These are the antecedent facts of the case:

Petitioner Commissioner of Internal Revenue is the official of the Republic of the Philippines charged with the duty of assessing and collecting national internal revenue taxes with office address

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[1] Annex A of Petition for Review *En Banc*
[2] Annex B of Petition for Review *En Banc*

at 5th Floor, Bureau of Internal Revenue, National Office Building, Agham Road, Diliman Quezon City. Respondent Aquafresh Seafoods, Inc., on the other hand, is a corporation organized and existing under Philippine laws with principal business address at Baybay, Roxas City.

Sometime on June 7, 1999, Philips Seafood Holdings Incorporated ("Philips") purchased from herein respondent Aquafresh Seafoods, Incorporated, two parcels of land, including improvements thereon, covered by Transfer Certificates of Titles (TCT) Nos. T-21799 and T-21804 situated at Barrio Banica, Roxas City, for the consideration of Three Million One Hundred Thousand Pesos (P3,100,000.00). On even date, respondent filed Capital Gains Tax ("CGT") Return/Application for Certificate Authorizing Registration, plus DST Declaration and paid the amounts of P186,000.00 and P46,500.00, respectively, representing CGT and Documentary Stamp Tax ("DST") due from the said sale.

Reports of undervaluation of the lots sold to Philips prompted the Special Investigation Division ("SID") of the BIR to conduct an ocular inspection over the properties. Finding sufficient basis for tax deficiency, Regional Director Leonardo Q.

Sacamos of Revenue Region ("RR") Iloilo City sent two separate Assessment Notices both dated September 15, 2000 apprising respondent of CGT and DST deficiencies in the sums of P1,372,171.46 and P356,267.62, respectively. He concluded that the lots are commercial with zonal valuation of P2,000.00 per square meter as per investigation of the SID. Respondent protested these assessments on October 1, 2000.

In a letter dated February 13, 2002, petitioner denied with finality, respondent's protest due to lack of legal basis and demanded the latter to settle its tax liability.

On March 19, 2002, respondent filed a Petition for Review docketed as CTA Case No. 6409 before the Court's First Division seeking the reversal of the denial of its protests against deficiency assessments for capital gains tax and documentary stamp tax, and for the cancellation of the said assessments.

In a Decision promulgated on December 22, 2004, the CTA First Division cancelled and set aside the deficiency assessments for capital gains and documentary stamp taxes in the amount of P1,728,439.08. However, respondent was ordered to pay the reduced amount of P394,197.22 as deficiency capital gains and documentary stamp taxes plus 20% delinquency interest computed from October 17, 2000 until fully paid pursuant to Section 249 of the 1997 Tax Code.

In arriving at the computed CGT and DST liabilities in the aggregate amount of P264,965.57 subject to surcharge and interest, the Court disagreed with herein petitioner that the subject lots should be classified as "commercial" based on the actual use thereof with zonal value of P2,000.00 per square meter at the time of sale. To quote:

> *"While our Tax Code vests unto the respondent several powers for the purposes of tax enforcement and administration, such powers shall not be capriciously, despotically and arbitrarily exercised. Zonal valuation was established with the objective of having an "efficient tax administration by minimizing the use of discretion in the determination of the tax base on the part of the administrator on one hand and the taxpayer on the other hand." Respondent cannot arrogate upon himself in classifying the subject properties as COMMERCIAL based on the actual use and apply the zonal value of P2,000.00 in determining the tax base and deficiency taxes of petitioner.*
>
> *In computing the tax liabilities of petitioner, the tax base shall be either the gross selling price or fair market value, whichever is higher. The fair market values of the subject lots sold, based on the existing zonal valuation in Roxas City, are as follows:*

"Lot No. 351-5-A	*5,857sq.m.*	*x*	*P650.00*	*P3,807,050.00*
Lot No. 3515-A-6-D	*385sq.m*	*x*	*P650.00*	*P 250,250.00*
				P4,057,300.00

> *Further, as established by evidence on record, there exist improvements on the lots sold which include water tank, fence and building on the date of sale with the following valuation:*

	Market Value
Building	*P2,910,647.35*
Fence	*492,480.00*
Water Tank	*129,582.18*
Total	*P3,532,709.53*

The Court does not subscribe to petitioner's claim that it should not be held liable for CGT and DST on the improvements found on the subject lots sold. While the subsequent owner Philips made considerable improvements or renovations on the building and converted the same as a processing plant in relation to the latter's business at the time the SID made an the investigation, petitioner admitted and respondent was able to prove that there was residential building, a fence and a water tank on the subject lots and it was paying real property as evidenced by Tax Declarations. Hence, the value of the improvements found on the lots sold shall be taken into consideration in determining the DST and CGT liabilities of petitioner.

As fair market values of the subject properties are higher than the selling price, petitioner is liable to pay deficiency CGT and DST, computed as follows:

Lots		*P4,057,300.00*
Improvements		*3,532,709.00*
Total		*P7,590,009.53*
6% CGT	*P455,400.57*	
Less CGT paid	*-243,430.00*	
CGT due		*P 211,970.57*
DST	*113,865.00*	
Less DST paid	*- 60,870.00*	
DST due		*P 52,995.00*
Total		*P 264,965.57"*[3]

Herein petitioner filed a Motion for Reconsideration of the said Decision and this was denied for lack of merit in a Resolution promulgated April 4, 2005. Hence, this Petition for Review *En Banc* on the following grounds:

[3] Decision, CTA Case No. 6409, December 22, 2004, pages 1-12

> *"I. THE COURT OF TAX APPEALS ERRED IN CLASSIFYING THE TWO LOTS SUBJECT OF SALE AS RESIDENTIAL LANDS WITH PHP650.00 PER SQUARE METER.*
>
> *II. THE HONORABLE COURT COMMITTED REVERSIBLE ERROR IN COMPUTING THE CAPITAL GAINS TAX DUE ON THE SALE USING THE AMOUNT OF PHP650.00 PER SQUARE METER AS TAX BASE.*
>
> *III. THE BIR IS ALLOWED TO CLASSIFY LANDS BASED ON THE ACTUAL USE, AS IN THIS CASE, THE COMPUTATION OF THE CORRECT CAPITAL GAINS AND DOCUMENTARY STAMP TAXES.*
>
> *IV. RESPONDENT'S ACTION RECLASSIFYING THE SUBJECT LOTS SEVERAL TIMES AS EVIDENCED BY THE TAX DECLARATIONS ISSUED, BEFORE AND AFTER THE SALE IS HIGHLY IRREGULAR AND TAINTED WITH FRAUD. "*

Being interrelated, the first, second and third grounds shall be jointly discussed. The crux of the controversy hinges on whether or not the Court correctly applied the fair market value based on the zonal valuation of a residential land as tax base in the computation of CGT and DST deficiencies.

Pursuant to Section 27 (D)(5) of the 1997 National Internal Revenue Code ("NIRC"), gains realized from sale, exchange or disposition of lands/or buildings which are not actively used in the business of the corporation and are treated as capital assets, are subject to a final tax of 6% based on the gross selling price or fair market value, whichever is higher, to wit:

> *"SEC. 27. Rates of Income Tax on Domestic Corporations. –*
>
> xxx xxx xxx
>
> *"(D)Rates of Tax on Certain Passive Incomes. –*
>
> xxx xxx xxx
>
> *"(5) Capital Gains Realized from the Sale, Exchange or Disposition of Lands and/or Buildings. – A final Tax of six percent (6%) is hereby imposed on the gain presumed to have been realized on the sale, exchange or disposition of lands and/or buildings which are not actually used in the business of a corporation and are treated as capital assets, based on the gross selling price or fair market value as determined in accordance with Section 6(E) of this Code, whichever is higher, of such lands and/or buildings."*

On the other hand, Documentary Stamp Tax on Deeds of Sale and Conveyances of real property is ascertained either on the (1) the amount of consideration or value received or contracted to be paid; or (2) the fair market value whichever is higher under Section 196 of the 1997 NIRC which provides:

> *"SEC. 196. Stamp Tax on Deeds of Sale and Conveyances of Real Property. - On all conveyances, deeds, instruments, or writings, other than grants, patents, or original certificates of adjudication issued by the Government , whereby any land, tenement or other realty sold shall be granted, assigned, transferred or otherwise conveyed to the purchaser, or purchasers, or to any other person or persons designated by such purchaser or purchasers, there shall be collected a documentary stamp tax, at the rates herein below prescribed, based on the consideration contracted to be paid for such realty or on its fair market value determined in accordance with Section 6(E) of this Code, whichever is higher: x x x"*

In the computation of both CGT and DST arising from the sale of real property, the basis is either the gross selling price or fair market value thereof as determined in accordance with Section 6(E) of the 1997 NIRC, whichever is higher.

Section 6(E) of the 1997 NIRC, provides thus:

> *" SEC.6 Power of the Commissioner to Make Assessments and Prescribe Additional Requirements for Tax Administration and Enforcement. -*
>
> *xxx xxx xxx*
>
> *" (E) Authority of the Commissioner to Prescribe Real Property Values - The Commissioner is hereby authorized to divide the Philippines into different zones or areas and shall, upon consultation with competent appraisers both from private and public sectors, determine the fair market value or real properties located in each zone or area. For purposes of computing any internal revenue tax, the value of the property shall be, whichever is higher of :*
>
> *"(1) the fair market value as determined by the Commissioner; or*
>
> *"(2) the fair market value as shown in the schedule of values of the Provincial and City Assessors."*

As can be gleaned from the foregoing legal provision, it is the Commissioner of Internal Revenue, herein petitioner, who is empowered to divide the entire Philippine archipelago into zones. Each zone or area has a corresponding valuation. <u>The zonal valuation of a real property must be identified to ascertain its fair market value</u>. The real property shall be appraised according to the fair market value as determined by the Commissioner or the fair market value as reflected in the schedule of values of the Provincial and City Assessors whichever is higher.

According to petitioner, the subject real properties are commercial/industrial with zonal valuation of P2,000.00 per square meter substantiated by the 1999 tax declarations and Certifications issued by the Metro Roxas Water District, Office of the City Planning and Development Coordinator, City Assessors Office and the BIR Revenue District Office, Roxas City. Allegedly, the investigation conducted by BIR Officer Jorge Pallon disclosed the presence of structures such as buildings, water tanks, enclosures and machineries inside the premises, which bolsters the fact that the lots were used in pursuit of commercial activities. Thus, petitioner claims that the real properties should be classified according to their actual use, which is commercial, as basis for zonal valuation thereof.

Respondent however contends that the law requires consultation with appraisers, from both the public and private sectors, in fixing the zonal valuation of the real properties. In the instant case, petitioner allegedly failed to confer with competent private appraisers. The 1995 Revised Zonal Valuation of Revenue District No. 72, as approved by the Finance Secretary classifying the property as residential, must be adhered to by the parties.

We agree with the respondent.

Although the authority to classify real properties for purposes of ascertaining fair market value is vested with the petitioner, Commissioner of Internal Revenue, this authority nevertheless, requires appropriate coordination with public and private appraisers. The Certifications issued by the Metro Roxas Water District of Roxas City, Office of the City Planning and Development Coordinator, City Assessors Office and the BIR-Revenue District Office, Roxas City, are not sufficient to establish the zonal valuation of subject property. Section 6(E) of the 1997 NIRC emphasizes that the Commissioner, " upon consultation with competent appraisers both from private and public sectors, is authorized to determine the fair market value or real properties located in each zone or area".

Zonal valuation is determined for the purpose of establishing a more realistic basis for real property valuation. Since internal revenue taxes, such as CGT and DST, are assessed on the basis of valuation, the zonal valuation existing at the time of the sale should be taken into account.[4] Hence, zonal valuation must be ascertained to arrive at the fair market value of real

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[4] Section 27 (D) (5) and Section 6 (E) of the NIRC and Hector M. De Leon and Hector S. De Leon Jr., The National Internal Revenue Code Annotated. 2003 Edition, Volume I, p. 133

property. And as between the fair market value determined by the petitioner or Provincial/City Assessor, the higher in value shall prevail.

In the case at bar, the conveyance of the real properties transpired on June 7, 1999. In arriving at the fair market, the CTA First Division aptly applied the prevailing zonal valuation at the time of the sale, which is P650.00 per square meter pertaining to residential zone under the 1995 Revised Zonal Values of Real Properties of RDO No. 72 for Barrio Banico.[5] Petitioner failed to prove any amendment effected on the 1995 Revised Zonal Value of Real Properties at the time of the sale.

The Revised Zonal Values of Real Properties was drafted by the petitioner, BIR personnel, representatives from the Department of Finance, National Tax Research Center, Institute of Philippine Real Estate Appraisers and Philippine Association of Realtors Board which duly satisfied the requirement of consultation with public and private appraisers.

Being higher in value, the CTA First Division did not err in using the fair market value instead of the gross selling

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[5] Ministry Order No. 21-86, amended by Department Order No. 13-89 and Department Order No. 11-92

price/consideration as tax base in the computation of the CGT and DST deficiencies.

Anent the fourth ground, petitioner contends that through the alleged connivance of the City Assessor's Office, respondent was able to change the lots' classification and valuation prior to the sale allegedly for the sole purpose of reducing or if not to evade payment of respondent's tax liabilities.

The Court is not persuaded with petitioner's argument.

Allegations of fraud being a serious charge, must be supported by clear and convincing evidence. Failing in this regard, such allegations of fraud must be dismissed .[6]

As earlier discussed, the determination of zonal values is exercised by the petitioner, together with public and private appraisers. Revenue Memorandum Order (RMO) No. 56-89 issued on October 24, 1989, provides certain procedures in the establishment of zonal value of real properties, to wit:

(1) The submission or review by the Revenue District Offices ("RDO") Sub-Technical Committee of the schedule of recommended

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[6] Commissioner of Internal Revenue vs. Javier, Jr., et. al., 199 SCRA 824; Commissioner of Internal Revenue vs. Yusay, et. al., 18 SCRA 757; Collector of Internal Revenue vs. Benipayo, 4 SCRA 182

zonal values to the Technical Committee on Real Property Valuation.

(2) The Technical Committee on Real Property Valuation evaluates the submitted schedule of recommended zonal values of real properties.

(3) Except in cases of correction or adjustment, the Technical Committee then finalizes the schedule and submits the same to the Executive Committee.

(4) Upon approval on the schedule of zonal values by the Executive Committee, the same is embodied in a Department Order for implementation and signed by the Secretary of Finance. Thereafter, the schedule takes effect fifteen (15) days after its publication in the Official Gazette.

The records do not show that Revenue Memorandum Order No. 56-89 was complied with by petitioner in revising the zonal valuation of subject real properties and therefore, the Revised Zonal Values of Real Properties by the City of Roxas must be followed.

Accordingly, We find no reversible error committed by the First Division of this Court in rendering the assailed Decision dated December 22, 2004, and the Resolution dated April 4, 2005.

WHEREFORE, premises considered, the Petition for Review is **DISMISSED** for lack of merit.

SO ORDERED.

ERLINDA P. UY
Associate Justice

WE CONCUR:

ERNESTO D. ACOSTA
Presiding Justice

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Associate Justice

LOVELL R. BAUTISTA
Associate Justice

CAESAR A. CASANOVA
Associate Justice

OLGA PALANCA-ENRIQUEZ
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 this Court *En Banc* before the case was assigned to the writer of the opinion of the Court.

ERNESTO D. ACOSTA
Presiding Justice