REPUBLIC OF THE PHILIPPINES
DEPARTMENT OF FINANCE
BUREAU OF INTERNAL REVENUE

Section 3(e) of RR 7-2003
OT-067-2023
JUN 06 2023

EMMANUEL G. HERBOSA
President and Chief Executive Officer
Development Bank of the Philippines
Makati Avenue, Makati City

Gentlemen:

This refers to your letter dated December 13, 2022 requesting for the amendment of Section 3(e) of Revenue Regulations (RR) No. 7-2003 in connection with the treatment of abandoned and idle properties acquired by a taxpayer engaged in the real estate business.

Section 3(e) of RR No. 7-2003 mandates that abandonment of real properties that formed part of the stock in trade of a taxpayer engaged in real estate business, will not convert the classification of the said properties from ordinary assets to capital assets, viz:

> "SECTION 3. Guidelines in Determining Whether a Particular Real Property is a Capital Asset or Ordinary Asset.
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> XXX
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> e. Treatment of abandoned and idle real properties. — Real properties formerly forming part of the stock in trade of a taxpayer engaged in the real estate business, or formerly being used in the trade or business of a taxpayer engaged or not engaged in the real estate business, which were later on abandoned and became idle, shall continue to be treated as ordinary assets. **Real property initially acquired by a taxpayer engaged in the real estate business shall not result in its conversion into a capital asset even if the same is subsequently abandoned or becomes idle.** (Emphasis supplied)"

It is represented that some of the Bank's clients from micro, small, and medium enterprise (MSME) sector have expressed concern that the subject provision has resulted in an unnecessary financial burden on MSMEs who must pay regular income tax upon their sale or disposal of the same instead of the lesser rate of capital gains tax.

In reply, please be informed that your request for amendment cannot be granted for lack of legal basis. It is worth noting that for real estate business, the sale of real properties is not just a one-time event but rather a regular and integral part of their business operations. As such, it is appropriate for real estate businesses to be subjected to regular income tax on their profits, rather than capital gains tax, which is generally intended for individuals who may have only occasional or sporadic capital gains.

Additionally, it would not be fair to allow real estate businesses to pay the lower capital gains tax rate while other businesses are subject to the higher income tax rate. This would create an unfair advantage for real estate businesses and could lead to an unequal playing field in the business world.

Finally, paying income tax on the sale of real properties is a matter of fairness and equity. It ensures that real estate businesses are contributing their fair share to the overall tax burden, and it helps to support the various public goods and services funded through taxes.

Please be guided accordingly.

Very truly yours,

ROMEO D. LUMAGUI, JR.
Commissioner of Internal Revenue
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