REPUBLIC OF THE PHILIPPINES
DEPARTMENT OF FINANCE
BUREAU OF INTERNAL REVENUE
Quezon City

RR No. 7-2003
BIR Ruling No. 634-17 BIR Ruling No. 480-2017 BIR Ruling No. 187-2017
VAT- 237-2021
JUL 12 2021

SUWA SHIPYARD & MACHINERIES CORP.
351 Governor's Drive, Sampaloc 3
Dasmariñas, Cavite

Attention: **Ms. Lika P. Mizukoshi**

Gentlemen:

This refers to your letter dated June 19, 2020 requesting, in effect, for a ruling on whether or not the sale of idle real property by **SUWA SHIPYARD & MACHINERIES CORP.** ("SUWA" for brevity) is subject to value-added tax (VAT).

Background

1. SUWA (TIN:) is a domestic corporation registered with the Securities and Exchange Commission (SEC) under Company Registration No. dated February 26, 1992[1] and with principal office address at 351 Governor's Drive, Sampaloc 3, Dasmariñas, Cavite.

2. The primary purpose for which SUWA was organized is to maintain and operate shipyard and to engage in the business of shipbuilding and ship repairing including equipping, remodelling, repairing, selling, exporting and importing of machineries, engines, parts, equipment, ships, boats, barges, vessels and crafts of any kind and sizes.[2]

3. SUWA has been non-operational since September 30, 1999 and end-dated for all tax types in 2009.[3] It is currently in the process of liquidation of its properties for its proper closure.

4. SUWA has two (2) real properties in its name, specifically a house and lot located at #50 Yellowbell Rd., Pilar Village, Las Piñas (Las Piñas property), and a lot in Dasmariñas, Cavite (Cavite property).

[1] See certified true copy of SEC Registration of SUWA.
[2] See certified true copy of Articles of Incorporation of SUWA.
[3] See RDO No. 54-A Certification dated September 21, 2020.

5. The Las Piñas property owned by SUWA is a residential house and lot originally intended to be an office of SUWA since its temporary office at the time was located in Anahaw St. in the same village. This was not pushed through after SUWA acquired the Cavite property where the permanent office was placed. The details of the afore-mentioned property are described, as follows:

Real Property	TCT No.	Tax Declaration Nos.	Area in sq.m.	Location
Land			280	Yellowbell Rd., Pilar Village, Las Piñas City
Improvement			69	Yellowbell Rd., Pilar Village, Las Piñas City

6. On November 19, 2019, SUWA sold the Las Piñas property.[4]

7. SUWA is in the process of transferring the title of the Las Piñas property to the new owners. Prior to the sale, Revenue District Office (RDO) No. 54-A (where SUWA is registered) advised SUWA that the sale of the Las Piñas property is not subject to VAT but to the capital gains tax (CGT) applying Section 3 (e) of Revenue Regulations (RR) No. 7-2003.

8. The documentary stamp tax (DST) on the sale of the Las Piñas property was paid on November 25, 2019.[5]

9. Upon paying the CGT[6] on November 25, 2019 and submitting the requirements to RDO No. 53-A (where the Las Piñas is located), SUWA was informed that Section 3 (e) of RR No. 7-2003, cannot apply since SUWA's TIN is still active in their system, and that SUWA must liquidate all assets within three (3) years of closure.

10. After RDO No. 53-A asked SUWA to amend the paid CGT to Expanded Withholding Tax (EWT), SUWA once again sought the advice of its RDO No. 54-A which directed SUWA to Revenue Region (RR) No. 8-B's Legal Division. The latter, however, referred SUWA to RR No. 9A-CaBaMiRo which has the same opinion as its RDO No. 54-A that the sale of the Las Piñas property is subject to CGT but not to VAT applying Section 3 (e) of RR No. 7-2003 and

[4] See copy of Deed of Absolute Sale between SUWA and Mrs. Ma. Lourdes A. San Juan and Mrs. Analen A. Chiefe.
[5] See copy of the BIR Form No. 2000-OT for the DST Return with the corresponding bank-validated deposit slip.
[6] See copy of the BIR Form No. 1706 for the CGT Return with the corresponding bank-validated deposit slip.

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recommended that SUWA seek the opinion of RDO No. 53-A and RR No. 8-B since the Las Piñas property is under their jurisdiction.

11. On December 19, 2019, SUWA filed a request letter on the matter. It has not received any formal reply. However, SUWA was informed that RR No. 8-B has sent a Memorandum[7] to RDO No. 53-A on February 25, 2020 stating that the sale of the Las Piñas property is subject to VAT pursuant to Section 3 (e) of RR No. 7-2003.

In reply, please be informed that the term "capital asset" as negatively defined in Section 39 (A)(1) of the National Internal Revenue Code of 1997 (Tax Code), as amended, 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 of the Tax Code, as amended, or real property used in trade or business of the taxpayer.

Section 39 (A)(1) of the Tax Code, as amended should be read together with RR No. 7-2003, particularly Section 3 (e), as follows:

> "SECTION 3. Guidelines in determining whether a particular real property is a capital asset or ordinary asset. —
>
> XXX XXX XXX
>
> 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.
>
> Provided however, that properties classified as ordinary assets for being used in business by a taxpayer engaged in business other than real estate business as defined in Section 2 (g) hereof are **automatically converted into capital assets** upon showing of proof that the same have not been used for more than two (2) years prior to the consummation of the taxable transactions involving said properties." (Emphasis and underscoring supplied)

[7] See copy of Memorandum to RDO No. 53A dated January 24, 2020.

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The above provision provides for the automatic conversion of real properties used in business by a taxpayer "engaged in business other than real estate business" from ordinary assets into capital assets upon showing of proof that the same have not been used in business for more than two (2) years prior to the consummation of the taxable transactions involving said properties. Thus, the two (2) important conditions set forth by RR No. 7-2003 for the automatic conversion of ordinary assets into capital assets are: 1) the assets were previously used in business by a taxpayer not engaged in real estate business; and 2) there must be a showing that the same have not been used in business for more than two (2) years.

The foregoing provision finds application in this case. SUWA is not engaged in the real estate business and it has already ceased its business operation in 1999, leaving the Las Piñas property idle since its acquisition and up to 2019 when the said property was sold as shown by the Certification dated June 1, 2021 issued by the Office of the Punong Barangay of Barangay Pilar, Las Piñas.

In view of the foregoing, it is the considered opinion of this Office that the real property, covered by TCT No. ', having complied with the conditions under Section 3 (e) of RR No. 7-2003, is classified as a capital asset of SUWA subject to CGT of 6% pursuant to Section 27(D)(5) of the Tax Code, as amended, and not to the creditable withholding tax. Moreover, the said property is exempt from 12% VAT, not being primarily held and offered for sale or lease to customers in the ordinary course of SUWA's trade or business, as provided under Section 109 (P) of the Tax Code, as amended.

This ruling is being issued on the basis of the foregoing facts as represented. However, if upon investigation, it will be ascertained that the facts are different, then this ruling shall be considered null and void.

Very truly yours,

CAESAR R. DULAY
Commissioner of Internal Revenue

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