September 5, 2018

BIR RULING NO. 1164-18

RR 13-85; RR 2-98; 000-00

Leah M. Quiambao
Assistant Secretary for Legal Affairs
Department of Transportation
The Columbia Tower
Brgy. Wack-Wack, Ortigas Avenue
1555 Mandaluyong City

Dear Asec. Quiambao,

This refers to your letter to Secretary Carlos G. Dominguez dated September 7, 2017, indorsed to this Office on January 16, 2018, requesting for opinion regarding the payment of taxes in connection with the transfer of 58 condominium units in The Columbia Tower, Brgy. Wack Wack, Ortigas Avenue, Mandaluyong, from LBP Leasing Corporation [now LBP Leasing and Finance Corporation (LLFC)] to the Department of Transportation (DOTr).

As represented, the DOTr sought the assistance of the Land Bank of the Philippines (LBP) to secure a new site for its national office. Since DOTr cannot borrow funds to acquire an office building, a lease-to-own option to be implemented by LLFC was agreed upon by the parties.

In 1997, DOTr and LLFC executed a Contract of Lease with Option to Purchase for the fifty-seven (57) condominium units (8,043 sq. m.) and ninety-five (95) parking slots. In May 2002, a Supplemental Contract was executed to cover the lease of one (1) additional condominium unit with two (2) parking slots.

In a meeting in March 2007, DOTr asked LLFC to hold the execution of the Deed of Absolute Sale over the subject properties as it still had to secure approval of the budget and funds for the payment of the capital gains tax (CGT) from the Department of Budget and Management (DBM).

LLFC claims that per the provisions of the Lease Contract with Option to Purchase, the DOTr shall shoulder *"all expenses related to the transfer including, but not limited to transfer tax, documentary stamp tax, and gross receipt adjustments."* For this reason, LLFC's computation of lease amortization to be paid by the DOTr did not factor a projection of the CGT to be paid for the eventual transfer of ownership from LLFC to

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DOTr. As regards the real property tax (RPT), in a meeting between the parties immediately after the full payment of the lease contracts in 2007, the DOTr assumed the responsibility to settle the RPT due thereon pending the execution of the Deed of Sale.

In May 2007, DOTr sent a letter to the Mandaluyong City Treasurer to inform the latter of the lease agreement with LLFC, the full payment of the lease, and to ask for assistance on the requirements for DOTr to claim exemption on the payment of the RPT over the 58 condominium units. The letter stated that *"DOTC is the beneficial owner of the condominium units although the titles are yet to be transferred to DOTC."*

In June 2008, the Mandaluyong City Treasurer replied to DOTr's letter and stated that *"the subject condominium units are still declared in the name of LBP Leasing Corporation, a private and taxable entity. Further, granting that the DOTC would be able to transfer the said condominium titles to their name, the exemption would commence the following quarter based on the registration date on the new titles . . ."*

Based on the foregoing, you now request for opinion on the following issues:

1) **Whether the DOTr is liable to pay the CGT by virtue of the provisions of the Contract of Lease with Option to Purchase; and**

2) **Whether the DOTr may be the party liable to pay the RPT as opposed to LLFC, but be exempted from paying being an agency of the national government.**

In reply, please be informed:

The DOTr is liable to pay the applicable taxes on the transfer of the condominium units.

Section 2 of Revenue Regulations (RR) No. 13-85 places the burden of paying the capital gains tax on the seller or the person who is presumed to have realized an income or gain from the sale of a capital asset, as follows:

> "SECTION 2. Persons Liable to the Final Capital Gains Tax. — (a) Every individual (including estates and trusts) whether resident or nonresident, shall be conclusively presumed to have realized capital gains from every sale or exchange or other disposition of real property classified as capital asset under Section 34(h) of the Tax Code and shall be subject to the final capital gains tax to be determined under Section 3 of these regulations. For purposes of this Section, the term "sale" shall include *pacto de retro* and other forms of conditional sale."

On the other hand, Section 2.57.3 (c) of Revenue Regulations (RR) No. 2-98, as amended by RR 11-2018, states that all government offices including government-owned or controlled corporations, as well as provincial, city and municipal governments and barangays are constituted as withholding agents for purposes of deducting and withholding the creditable tax on the gross selling price or total amount of consideration

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or the fair market value determined in accordance with Section 6 (E) of the 1997 Tax Code, as amended, whichever is higher, paid to the seller/owner for the sale, exchange or transfer of real property, other than capital asset. The obligation to withhold is imposed upon the buyer-payor of income although the burden of tax is really upon the seller-income earner/payee; hence, unjustifiable refusal of the latter to be subjected to withholding shall be a ground for the mandatory audit of all internal revenue tax liabilities, as well as the imposition of penalties pursuant to Section 275 of the Tax Code, as amended, upon verified complaint of the buyer-payor.

The tax consequences of the sale transactions of LLFC depend on the classification of the properties that are subject of the sale.

Section 27 (D) (5) of the Tax Code of 1997, as amended, imposes a final tax of 6% on the gain presumed to have been realized on the sale, exchange or disposition of land and/or building which are actually not used in the business of a corporation and are treated as capital assets, based on the gross selling price, or fair market value, whichever is higher.

Only such real properties held primarily for sale or lease in the ordinary course of its business, or which would be properly included in the inventory of such taxpayer, if on hand at the close of the taxable year, or used in its trade or business are appropriately classified as ordinary assets. Otherwise stated, real properties other than those enumerated under Section 39 (A) (1) of the Tax Code and Section 2 (b) of Revenue Regulations (RR) No. 7-2003 [1] will be properly treated as capital assets.

Considering that the subject properties are held by LLFC primarily for sale or lease in the ordinary course of its business, the same shall be considered as ordinary assets. Thus, the sale or disposition of the subject real properties by LLFC is not subject to capital gains tax as imposed under Section 27 (D) (5) of the Tax Code of 1997, as amended, but to creditable withholding tax pursuant to Section 2.57.2 (J) of RR No. 2-98, as amended by RR 11-2018.

DOTr, being a government office, is considered a withholding agent required to deduct and withhold the creditable withholding tax.

As regards the issue on whether or not the burden of tax may be shifted to DOTr, this Office has recognized the validity of the agreement between parties to the contract whereby taxes arising from or by reason of the contract shall be shouldered by a party not legally liable therefor as having the force of law between the parties based on Article 1306 of the Civil Code of the Philippines which provides:

> *"Art. 1306. The Contracting parties may establish such stipulations, clauses, terms and conditions as they may deem convenient, provided they are not contrary to law, morals, good customs, public order, or public policy."*

In the instant case, the agreement was freely entered into by and between DOTr

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and LLFC. Thus, the stipulation in the Contract of Lease with Option to Purchase whereby the former shall be the one to pay the transfer tax, not being contrary to law, morals, good customs, public order or public policy, has the force of law between the parties and should be complied with in good faith. *(BIR Ruling No. 019-03 dated November 28, 2003)*

RPT is not within the jurisdiction of BIR.

The issue on whether the DOTr may be exempted from paying the RPT, being an agency of the national government, must be addressed to the Bureau of Local Government Finance, RPT being outside the jurisdiction of the Bureau of Internal Revenue.

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,

(SGD.) CAESAR R. DULAY
Commissioner of Internal Revenue

Footnotes

1. Note from the Publisher: Copied verbatim from the official copy. Missing Footnote text.

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