Supreme Court E-Library

THIRD DIVISION

[G.R. No. 249668; July 13, 2022]

CITY OF DAVAO AND BELLA LINDA N. TANJILI, IN HER OFFICIAL CAPACITY AS CITY TREASURER OF DAVAO CITY, *Petitioners*, *v.* **ARC INVESTORS, INC.,** *Respondent.*

R E S O L U T I O N

INTING, *J.*:

Before the Court is a Petition for Review on *Certiorari*[1] assailing the Decision[2] dated January 29, 2019 and the Resolution[3] dated September 11, 2019 of the Court of Tax Appeals, *En Banc* (CTA *En Banc*) in CTA EB No. 1589, which sustained the CTA Division in canceling and setting aside the assessment against respondent ARC Investors, Inc. (ARCII) for local business taxes.

The Antecedents

ARCII is a domestic corporation duly organized and existing under the laws of the Philippines whose primary purpose under its Articles of Incorporation (AOI) reads:

"To purchase, subscribe for, or otherwise acquire and own, hold, use, sell, assign, transfer, mortgage, pledge, exchange, or otherwise dispose of real or personal property of every kind and description, including

---

1 *Rollo*, pp. 11-25.

2 Id. at 27-48. Penned by Associate Justice Catherine T. Manahan; concurred in by Presiding Justice Roman G. Del Rosario and Associate Justices Erlinda P. Uy, Esperanza R. Fabon-Victorino, Cielito N. Mindaro-Grulla, and Ma. Belen M. Ringpis-Liban; and dissented to by Associate Justice Juanito C. Castañeda, Jr.

3 Id. at 50-56. Penned by Associate Justice Catherine T. Manahan; concurred in by Presiding Justice Roman G. Del Rosario and Associate Justices Esperanza R. Fabon-Victorino, Cielito N. Mindaro-Grulla, Ma. Belen M. Ringpis-Liban, Jean Marie A. Bacorro-Villena, and Maria Rowena Modesto-San Pedro; and dissented to by Associate Justice Juanito C. Castañeda, Jr.; Associate Justice Erlinda P. Uy, on leave.

Supreme Court E-Library

shares of stock, voting trust certificates for shares of capital stock, bonds, debentures, notes, evidences of indebtedness, and other securities, contracts, or obligations of any corporation or corporations, association or associations, domestic or foreign, and to pay therefor in whole or in part in cash by exchanging therefor stocks, bonds, or other evidences of indebtedness or securities, contracts, or obligation, to receive, collect and dispose of the interest, dividends and income arising from such property, and to possess and exercise in respect thereof, all the rights, powers and privileges of ownership, including all voting powers on any stocks so owned; and to do every act and thing covered generally by the denomination "[sic] holding corporation and specially to direct the operations of other corporations through the ownership of stock therein, provided however that the Corporation shall not act as an investment company or a securities broker and/or dealer nor exercise the functions of a trust corporation."[4]

In 2010, ARCII earned an amount of ₱801,634,060.07, by way of dividends from its preferred shares of stocks in San Miguel Corporation (SMC) and interests on its money market placements[5] (collectively, dividends and interests), computed as follows:

Nature of Income	Amount
Dividends from ARCI's SMC [Shares]	₱792,670,200.00
Interest Income from ARCI's Money Market Placements	₱8,963,860.07
Total	₱801,634,060.07[6]

On January 20, 2014, the City of Davao and Bella Linda N. Tanjili, in her official capacity as City Treasurer of Davao (petitioners) assessed ARCII of local business taxes (LBT) in the amount of ₱4,381,431.90, equivalent to 0.55% of the foregoing dividends and interests for the third and fourth quarters of 2011.[7]

---

4 As culled from the CTA *En Banc* Decision dated January 29, 2019. Id. at 28-29.

5 Id. at 57.

6 Id.

7 Id. at 29, 57.

Supreme Court E-Library

On March 21, 2014, ARCII filed with the City Treasurer of Davao a written administrative protest characterizing the assessment as erroneous and illegal. Following petitioners' alleged inaction on the protest, ARCII filed with Branch 16, Regional Trial Court (RTC) of Davao City, a petition for review questioning the LBT assessment.[8]

First, ARCII contended that it is not a bank or financial institution, upon which LBT may be imposed by cities under Section 133(a)[9] of Republic Act No. (RA) 7160, or the Local Government Code (LGC). Invoking its AOI "expressly prohibit[ing] it from acting as an investment company or a securities broker and/or dealer," ARCII asserted that it is not engaged in the business of investing, reinvesting, or trading securities and/or foreign exchange.[10]

Second, ARCII underscored that its receipt of dividends and interests is merely incidental to, or as a consequence of, its ownership of SMC shares and money market placements; hence, not constitutive of "business activity" as may be subject to LBT under the LGC.[11]

Third, ARCII invoked Section 27(D)[12] of RA 8424, as amended, or the National Internal Revenue Code of 1997 (NIRC),

---

[8] Id. at 57.

[9] Section 133. *Common Limitations on the Taxing Powers of Local Government Units*. — Unless otherwise provided herein, the exercise of the taxing powers of provinces, cities, municipalities, and barangays shall not extend to the levy of the following:

(a) Income tax, *except* when levied on *banks and other financial institutions*;

x x x x (Italics in the original and supplied).

[10] *Rollo*, pp. 58-60.

[11] Id. at 60-61.

[12] Section 27. *Rates of Income Tax on Domestic Corporation*. –

x x x x

(D) Rates of Tax on Certain Passive Incomes. –

x x x x

(4) Intercorporate Dividends. – *Dividends received by a domestic corporation from another domestic corporation shall not be subject to tax.*

x x x x (Italics Supplied).

Supreme Court E-Library

providing that dividends received by a domestic corporation from another domestic corporation are not subject to tax.[13]

Lastly, ARCII cited the ruling of the Court in the case of *COCOFED v. Republic of the Philippines*,[14] characterizing the Coconut Industry Investment Fund (CIIF) block of SMC shares as government-owned funds partaking of a public character, hence not subject to local taxation.[15]

The Ruling of the RTC

In its Order[16] dated October 15, 2014, the RTC denied ARCII's petition.

The RTC ruled that ARCII is engaged in business as a financial intermediary. Treating ARCII's dividends and interests earned from money market placements as principal sources of income in line with the primary purpose stated in its AOI, the RTC held that the same are subject to LBT under Section 143(f),[17] in relation to Section 151,[18] of the LGC.[19]

---

[13] *Rollo*, pp. 58-60.

[14] 679 Phil. 508 (2012).

[15] *Rollo*, p. 61.

[16] Id. at 57-69. Penned by Presiding Judge Emmanuel C. Carpio.

[17] Section 143. *Tax on Business*. – The municipality may impose taxes on the following businesses:

x x x x

(f) On banks and *other financial institutions*, at a rate not exceeding fifty percent (50%) of one percent (1%) on the gross receipts of the preceding calendar year derived from interest, commissions and discounts from lending activities, income from financial leasing, dividends, rentals on property and profit from exchange or sale of property, insurance premium. x x x x (Italics supplied).

[18] Section 151. *Scope of Taxing Powers*. – Except as otherwise provided in this Code, the city may levy the taxes, fees, and charges which the province or municipality may impose: *Provided, however*, That the taxes, fees and charges levied and collected by highly urbanized and independent component cities shall accrue to them and distributed in accordance with the provisions of this Code.

The rates of taxes that the city may levy may exceed the maximum rates allowed for the province or municipality by not more than fifty percent (50%) except the rates of professional and amusement taxes.

[19] *Rollo*, pp. 66-69.

Supreme Court E-Library

Following the denial of its motion for reconsideration, ARCII filed a petition for review with the CTA Division questioning the ruling of the RTC.[20]

The Ruling of the CTA

In its Decision[21] dated August 16, 2016, the CTA Division reversed the ruling of the RTC and consequently cancelled the questioned assessment of LBT against ARCII. Failing to obtain reconsideration thereof, petitioners filed a petition for review with the CTA *En Banc*.

In the challenged Decision dated January 29, 2019, the CTA *En Banc* affirmed the ruling of the CTA Division, and held that ARCII cannot be considered either as a financial intermediary or a non-bank financial intermediary (NBFI), based on the following reasons: *first*, respondent is not authorized by the Bangko Sentral ng Pilipinas to perform quasi-banking activities;[22] *second*, ARCII's function, as stated in its AOI, does not relate *principally* to NBFI activities;[23] and, *third*, there was no showing that the relevant functions performed by ARCII were on a regular and recurring basis, as opposed to being merely isolated.[24] Lastly, the CTA *En Banc* cited its ruling in the case of *Michigan Holdings, Inc. v. The City Treasurer of Makati City*[25] that a holding company is not among the entities enumerated as "banks and other financial institutions" under Section 131(e)[26] of the LGC.[27]

---

[20] Id. at 30.

[21] Not attached to the *rollo*, but referenced in the CTA *En Banc* Decision dated January 29, 2019. Id. at 30-31.

[22] *Rollo*, p. 39.

[23] Id.

[24] Id.

[25] CTA EB No. 1093 (CTA AC No. 99) dated June 17, 2015.

[26] Section 131. *Definition of Terms*. — When used in this Title, the term:

x x x x

(e) "Banks and other financial institutions" include non-bank financial intermediaries, lending investors, finance and investment companies, pawnshops, money shops, insurance companies, stock markets, stock

Supreme Court E-Library

Petitioners filed a motion for reconsideration, but CTA *En Banc* denied it in its Resolution dated September 11, 2019.

Hence, the petition.

The Issue

The core issue for resolution is whether ARCII is an NBFI subject to LBT under Section 143(f), in relation to Section 151, of the LGC.

The Court's Ruling

The Court holds in the *negative*.

Indeed, local government units have the power to impose LBT on the *privilege of doing business* within their territorial jurisdictions.[28] The term "doing business" contemplates some "trade or commercial activity regularly engaged in as a means of livelihood or with a view to profit."[29] Here, petitioners assessed ARCII of LBT based on Section 143(f), in relation to Section 131(e) of the LGC. The provisions read:

Section 143. *Tax on Business*. — The municipality may impose taxes on the following businesses:

x x x x

(f) On banks and *other financial institutions*, at a rate not exceeding fifty percent (50%) of one percent (1%) on the gross receipts of the preceding calendar year derived from interest, commissions and discounts from lending activities, income from financial leasing, dividends, rentals on property and profit from exchange or sale of property, insurance premium. (Emphasis supplied)

Section 131. *Definition of terms.* – x x x

x x x x

---

brokers and dealers in securities and foreign exchange, as defined under applicable laws, or rules and regulations thereunder:
x x x x

[27] *Rollo*, p. 40.

[28] See *The City of Manila v. Coca-Cola Bottlers Phils., Inc.*, 612 Phil. 609, 623-624 (2009).

[29] See Section 131(d) of the LGC.

Supreme Court E-Library

(e) "Banks and other financial institutions" include *non-bank financial intermediaries*, lending investors, finance and investment companies, pawnshops, money shops, insurance companies, stock markets, stock brokers and dealers in securities and foreign exchange, as defined under applicable laws, or rules and regulations thereunder[.] (Emphasis supplied)

Under Section 143(f), the persons liable to pay LBT are banks or other financial institutions by virtue of the nature of their business. LBT are imposed on their gross receipts from "*interest*, commissions and discounts from lending activities, income from financial leasing, *dividends*, rentals on property and profit from exchange or sale of property, insurance premium." In order to be considered as an NBFI under the LGC, in relation to the NIRC and pertinent banking laws and regulations, the following requisites must concur:[30]

a. The person or entity is authorized by the BSP to perform quasi-banking functions;

b. The *principal functions* of said person or entity include the *lending, investing or placement of funds* or evidences of indebtedness or equity deposited to them, acquired by them, or otherwise coursed through them, either for their own account or for the account of others; and

c. The person or entity must perform any of the following functions on a *regular and recurring, not on an isolated basis*, to wit:

1. Receive funds from one (1) group of persons, irrespective of number, through traditional deposits, or issuance of debt or equity securities; and make available/lend these funds to another person or entity, and in the process acquire debt or equity securities;

2. Use principally the funds received for acquiring various types of debt or equity securities;

3. Borrow against, or lend on, or buy or sell debt or equity securities.[31] (Italics supplied, citations omitted)

Based on the foregoing parameters, ARCII, in so owning SMC preferred shares of stock, as well as deriving dividends and

---

[30] See *City of Davao v. Randy Allied Ventures, Inc.*, G.R. No. 241697, July 29, 2019.

[31] Id.

Supreme Court E-Library

interests therefrom, *cannot be said to be "doing business" as a bank or other financial institution*.

It bears underscoring that in *COCOFED v. Republic of the Philippines*,[32] the Court held that ARCII is one of the 14 CIIF holding companies established to own and hold SMC shares of stock. Therein, the Court underscored that the SMC preferred shares held by CIIF holding companies and the derivative dividends or increments, are considered assets owned by the National Government,[33] which shall be used *only* for the benefit of the coconut farmers and for the development of the coconut industry.[34] Consequently, pursuant to this underlying purpose distinct to CIIF holding companies, the *management of dividends* derived from the SMC preferred shares of stock, including *placing them in interest yielding market*, does not *of itself* amount to doing business, either as a bank or other financial institution, *i.e.*, an NBFI.[35]

In *City of Davao v. Randy Allied Ventures, Inc.*,[36] the Court distinguished a holding company from a financial intermediary for purposes of local business taxation, as follows:

---

[32] Supra note 14.

[33] "Since the CIIF companies and the CIIF block of SMC shares were acquired using coconut levy funds – funds, which have been established to be public in character – it goes without saying that these acquired corporations and assets ought to be regarded and treated as government assets. Being government properties, they are accordingly owned by the Government, for the coconut industry pursuant to currently existing laws." Id. at 621.

[34] [T]he State's avowed policy or purpose in creating the coconut levy fund is for the development of the entire coconut industry, which is one of the major industries that promotes sustained economic stability, and not merely the livelihood of a significant segment of the population. Accordingly, We sustain the ruling of the Sandiganbayan in CC No. 0033-F that the CIIF companies and the CIIF block of SMC shares are public funds necessary owned by the Government. We, however, modify the same in the following wise: These shares shall belong to the Government, which shall be used only for the benefit of the coconut farmers and for the development of the coconut industry. Id. at 622.

[35] Supra note 17.

[36] Supra note 30.

Supreme Court E-Library

[T]here is a stark distinction between a holding company and a financial intermediary as contemplated under the LGC, in relation to other laws. A "'holding company' is 'organized' and is basically conducting its business by *investing substantially in the equity securities* of another company for the *purpose of controlling their policies* (as opposed to directly engaging in operating activities) and *'holding' them* in a conglomerate or umbrella structure along with other subsidiaries." While holding companies may partake in investment activities, this does not *per se* qualify them as financial intermediaries that are actively dealing in the same. Financial intermediaries are regulated by the BSP because they deal with public funds when they offer quasi-banking functions. On the other hand, a holding company is not similarly regulated because *any investment activities it conducts are mere incidental operations, since its main purpose is to hold shares for policy-controlling purposes*.[37] (Emphasis supplied, citations omitted).

The primary test for the distinction contemplates "*regularity of function, not on an isolated basis, with the end in mind for self-profit*."[38] In the case, ARCII's placement of dividends derived from its SMC shares in the market *incidentally* earning interests, does not negate the corporation's *restricted* underlying purpose as a CIIF holding company — *i.e.*, to manage the dividends of SMC preferred shares for and on behalf of the government — as would convert it into an active investor or dealer in securities. Lacking in the element of *regularity or recurrence for the purpose of earning a profit*, ARCII's money market placements cannot amount to "doing business" as an NBFI,[39] as may be subject to local business taxation.

Lastly, the Court finds *Bureau of Local Government Finance Opinion* dated February 22, 2011 as enlightening on the matter, thus:

It is clear from [Section 143(f) of the LGC] that unless imposed on banks and other financial institutions, any tax imposed on interest, dividends, and gains from sale of shares of non-bank and non-financial institutions assume the nature of income tax. The reason for this is evident: *while banks and other financial institutions derive gross receipts*

---

[37] Id.

[38] Id.

[39] See *City of Davao v. AP Holdings, Inc.*, G.R. No. 245887, January 22, 2020.

Supreme Court E-Library

in the ordinary course of their business as financial institutions, the same cannot be said for non-bank and non-financial institutions. As to the latter, *interest, dividends, and gains from sale of shares are merely passive investment income*.[40]

In the same Opinion, the Bureau of Local Government Finance added that the definition of "gross sales or receipts" under Section 131(n)[41] of the LGC neither includes nor mentions passive income (*i.e.*, dividend income received from another domestic corporation) as one of those that are considered part or forming part of the *gross sales or receipts*; hence, such income is not subject to local business tax.

In *fine*, the City of Davao acted beyond its taxing authority in assessing ARCII the questioned LBT on the premise that it is an NBFI.

WHEREFORE, the petition is **DENIED**. The Decision dated January 29, 2019 and the Resolution dated September 11, 2019 of the Court of Tax Appeals, *En Banc* in CTA EB No. 1589 are **AFFIRMED**.

SO ORDERED.

Caguioa (Chairperson), Gaerlan, Dimaampao, and *Singh, JJ.*, concur.

APPEARANCES OF COUNSEL

Francis A. Fernandez & Osmundo P. Villanueva for petitioners.
Carag Zabalero Llamado & Abiera for respondent.

---

[40] Emphasis supplied.

[41] Section 131. *Definition of Terms*. — When used in this Title, the term:

x x x x

(n) "Gross Sales or Receipt" include the total amount of money or its equivalent representing the contract price, compensation or service fee, including the amount charged or materials supplies with the services and deposits or advance payments actually or constructively received during the taxable quarter for the services performed or to be performed for another person excluding discounts if determinable at the time of sales, sales return, excise tax, and value-added tax (VAT);

x x x x