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Tax liability on nonredemption of property

Accumulation of debt is inevitable in any developing country like ours. From these debts, loans are created as well as mortgages. Most of the time, a simple Juan may not be able to pay his indebtedness and in the end he will be deprived of his beloved property in what we call as foreclosure or involuntary sale.

Foreclosure is the remedy available to the mortgagee (creditor) by which he may subject the mortgaged property to an involuntary sale, also called an auction sale, in order to satisfy the unpaid obligation of the mortgagor.

During the foreclosure sale, the mortgaged property will be sold to the highest bidder. A certificate of registration will then be issued and duly registered with appropriate Registry of Deeds.

However, under our laws, a mortgagor may still redeem the property sold at any time during the redemption period.

For extrajudicial sale, a mortgagor has one year from the date of registration of the certificate of sale to Registry of Deeds to redeem the subject property.

But for juridical mortgagors, such as corporations and partnerships, their right of redemption period is within three months after the date of foreclosure of the property but not after the registration of the certificate of foreclosure sale with the Registry of Deeds. This is in accordance with Section 47 of the General Banking Law of 2000.

For judicial foreclosure, the mortgagor/debtor has 90 to 120 days to pay the judgment debt after the finality of judgment but prior to its confirmation in order to redeem the subject property. This is called equity of redemption.

Once the statutory redemption period has prescribed and the owner or mortgagor failed to redeem the subject property within the period, taxes must be paid based on the foreclosed property.

The Revenue Regulation (RR) 9-2012 issued by the Bureau of Internal Revenue, simply states that there will be taxes that have to be dealt with for nonredemption of foreclosed property.

Under RR 9-2012, regardless of the type of proceedings and personality of mortgagees, if the property sold is a capital asset to the mortgagor or owner, then Capital Gains Tax (CGT) shall be imposed in accordance with Sections 24(D)(1) and 27(D)(5) of the Tax Code. If it is an ordinary asset, then Creditable Withholding Tax (CWT) shall be imposed under Section 57 of the Tax Code and Revenue Regulation 2-98, as amended.

Ordinary assets are assets which include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer 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 3 of the Tax Code; or real property used in trade or business of the taxpayer. All other assets are considered capital assets.

Although the tax burden or the obligation to pay the tax is on the mortgagor/seller/owner of the auctioned property, it is the responsibility of the buyer of the property to withhold the capital gains tax or the creditable withholding tax, and remit this with the Bureau of Internal Revenue, as the case may be.

In RMC 58-2008, it is required that 30 days from the expiration of the applicable redemption period, the buyer shall file the capital gains tax return and remit the said tax with the bureau. If it is a creditable withholding tax, the buyer of the subject property shall file the corresponding return and remit the said tax within 10 days following the end of the month after the expiration of the applicable redemption period, provided that, for taxes withheld in December, the creditable withholding tax return shall be filed and remitted on or before January 15 of the following year.

Also from RMC 58-2008, if the subject property sold is under the circumstances which warrant the imposition of value-added tax (VAT), this must be paid to the bureau by the VAT-registered owner/mortgagor on or before the 20th day or 25th day, whichever is applicable, of the month following the month when the right of redemption prescribes.

As for documentary stamp tax, the return shall be filed and the tax must be paid within five days after the end of the month when the redemption period expires.

In RMC 55-2011, it is stated that for purposes of reckoning the one-year redemption period on the foreclosed asset of natural persons and the period within which to pay capital gains tax or creditable withholding tax and documentary stamp tax on the foreclosure of real estate mortgage, the same shall be reckoned from the date of registration of the sale in the Office of the Register of Deeds.

As regards to the right of redemption of juridical persons in an extrajudicial foreclosure, it shall be reckoned from the date of approval by the executive judge.

Under RR 9-2012, the tax base for the capital gains tax, creditable withholding tax, value-added tax and documentary stamp tax shall either be the consideration (which is the bid price of the highest bidder or the buyer) or the fair market value or the zonal value pursuant to Section 6(E) of the Tax Code, whichever is higher.

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