Republic of the Philippines
COURT OF TAX APPEALS
Quezon City

SECOND DIVISION

SAN ROQUE POWER CORPORATION, Petitioner,	**C.T.A. CASE NO. 6372**
	Members:
- versus -	**CASTAÑEDA, JR.**, *Chairman* **UY**, and **PALANCA-ENRIQUEZ**, JJ.
THE COMMISSIONER OF INTERNAL REVENUE, Respondent.	Promulgated: SEP 09 2005

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DECISION

CASTAÑEDA, JR., J.:

This case involves a claim for refund or issuance of a tax credit certificate in the total amount of P52,900,550.67 allegedly representing unutilized input VAT paid on purchases of capital goods and other taxable goods and services attributable to zero-rated sales.

The antecedent facts as culled from the records of the case are as follows:

Petitioner is a domestic corporation duly organized and existing under and by virtue of the laws of the Philippines with principal office at Barangay San Roque, San Manuel, Pangasinan.

In October 1997, petitioner was incorporated to design, construct, erect, assemble, own commission(ed) and operated power-generating plants and related facilities pursuant to and under contract with the Government of the Republic of the Philippines, or any subdivision, instrumentality or agency thereof, or any government-owned or controlled corporation, or other entity engaged in the development, supply, or distribution of energy.

As a seller of services, petitioner is duly registered with the Bureau of Internal Revenue (BIR) as a value-added tax (VAT)- registered taxpayer under TIN/VAT Registration No. 005-017-501. Likewise, petitioner is registered with the Board of Investments (BOI) on a preferred pioneer status, to engage in the design, construction, erection, assembly, as well as to own, commission, and operate electric power-generating plants and related activities, for which it was issued Certificate of Registration No. 97-356 on February 11, 1998.

On October 11, 1997, petitioner entered into a Power Purchase Agreement (PPA) with the National Power Corporation (NPC) to develop the hydropotential of the Lower Agno River and generate additional power and energy for the Luzon Power Grid, by building the San Roque Multi-Purpose Project located in San Manuel, Pangasinan. The PPA provides, among others, that petitioner shall be responsible for the design, construction, installation, completion, testing, and commissioning of the Power Station and shall operate and maintain the same, subject to NPC instructions. During the co-operation period of twenty-five (25) years commencing from the completion date of the Power Station, NPC will take and pay for all electricity available from the Power Station. In other words, the electricity to be generated by the Power Station will be sold to and purchased by NPC in its entirety.

On January 25, 2000, petitioner validly filed its quarterly VAT return for the period covering October 1 to December 31, 1999.

On September 11, 2000, petitioner filed with the BIR a claim for refund in the amount of P52,900,550.67, representing unutilized VAT input taxes paid on purchases of capital goods and other taxable goods and services for the period October 1 to December 31, 1999.

Unable to find any response from the respondent and in order to stop the running of the two-year prescriptive period, petitioner elevated the case through a Petition for Review with this Court on December 26, 2001.

By way of an Answer filed on January 30, 2002, respondent asserted the following Special and Affirmative Defenses:

4. Petitioner's alleged claim for refund is subject to administrative routinary investigation/examination by the Bureau;

5. The amount of P52,900,550.67 being claimed by petitioner as alleged unutilized input VAT on purchases of capital goods and other taxable goods and services for the period October 1 to December 31, 1999 was not properly documented;

6. In an action for refund, the burden of proof is on the taxpayer to establish its right to refund, and failure to sustain the burden is fatal to the claim for refund/credit;

7. Petitioner must show that it has complied with the provisions of Sections 204(C) and 229 of the Tax Code on the prescriptive period for claiming tax refund/credit;

8. Claims for refund are construed strictly against the claimant for the same partake the nature of exemption from taxation.

To support its claim, petitioner submitted numerous documents and likewise presented witnesses to identify the same. Respondent, on the other hand, submitted the case for decision based on the pleadings. Therefore, on April 28, 2005, the Court issued a resolution and considered the case submitted for decision sans memorandum of respondent.

ISSUES

As mutually agreed by the parties on April 4, 2002, the following are the issues to be resolved issues in this case:

1. Whether or not petitioner has incurred input taxes in the amount of P52,900,550.67, on its purchases of capital goods and other taxable goods and services;

2. Whether or not the accumulated input VAT of P52,900,550.67 arising from petitioner's purchases of capital goods and other taxable goods and services for the period October 1 to December 31, 1999 are properly substantiated by VAT invoices and receipts and other documents evidencing the payment of VAT;

3. Whether or not petitioner has applied or utilized its accumulated input VAT incurred on the purchases of capital goods and other taxable goods and services for the period October 1 to December 31, 1999 to the succeeding quarters;

4. Whether or not petitioner is entitled to a tax credit certificate/refund in the amount of P52,900,550.67 representing unutilized input VAT paid on its purchased of capital goods and other taxable goods and services for the period October 1 to December 31, 1999.

THIS COURT'S RULING

Petitioner's claim for refund is based on Section 112(A) and (B) of the National Internal Revenue Code of 1997 (NIRC), to wit:

"SEC. 112. Refunds or Tax Credits of Input Tax. –

(A) *Zero-rated or Effectively Zero-rated Sales.* – Any VAT-registered person, whose sales are zero-rated or effectively zero-rated may, within two (2) years after the close of the taxable quarter when the sales were made, apply for the issuance of a tax credit certificate or refund of creditable input tax due or paid attributable to such sales, except transitional input tax, to the extent that such input tax has not been applied against output tax: *Provided, however,* That in the case of zero-rated sales under Section 106 (A)(2)(a)(1), (2) and (B) and Section 108 (B)(1) and (2), the acceptable foreign currency exchange proceeds thereof had been duly accounted for in accordance with the rules and regulations of the *Bangko Sentral ng Pilipinas* (BSP):

> *Provided, further,* That where the taxpayer is engaged in zero-rated sale and also in taxable or exempt of goods or properties or services, and the amount of creditable input tax due or paid cannot be directly and entirely attributed to any one of the transactions, it shall be allocated proportionately on the basis of the volume of sales.
>
> (B) *Capital Goods.* – A VAT-registered person may apply for the issuance of a tax credit certificate or refund of input taxes paid on capital goods imported or locally purchased, to the extent that such input taxes have not been applied against output taxes. The application may be made only within two (2) years after the close of the taxable quarter when the importation or purchase was made *(Underscoring Ours).*"

By virtue of the Power Purchased Agreement (PPA) entered into by petitioner with the NPC, central is the provision of Section 13 of Republic Act No. 6395, otherwise known as the Revised NPC Charter. To quote:

> "The Corporation shall be non-profit and shall devote all its returns from its capital investment as well as excess revenues from its operation, for expansion. To enable the Corporation to pay its indebtedness and obligations in furtherance and effective implementation of the policy enunciated in Section 1 of this Act, the Corporation, including its subsidiaries, is hereby declared exempt from all taxes, duties, fees, imposts, as well as costs and service fees, including filing fees, appeal bonds, supersedeas bonds, in any court or administrative proceedings." (*Underscoring supplied)*

Applying the aforequoted provision and as consistently ruled by this Court, NPC is exempt from all taxes, direct or indirect. And pursuant to Section 108(B)(3) of the 1997 NIRC, sale of services by a VAT registered entity to NPC is subject to zero percent VAT. Thus, the sale of power by petitioner to NPC is subject to VAT at zero percent and as confirmed by VAT Ruling No. 015-99 dated February 12, 1999.

On January 25, 2000, petitioner filed its 4th Quarterly VAT Return for taxable year 1999 declaring the following information *(Exhibits A, A-1 to A-7, K, K-1 and K-2)*:

		VAT Output Tax
Taxable Sales		P -
		VAT Input Tax
Input Tax Carried Over From Previous Quarter		P314,508,685.49
Domestic Purchases	P529,005,506.75	52,900,550.67
Total Available Input Tax		P367,409,236.16
Less: Any VAT Return/TCC Claimed		314,508,685.49
Total Amount Payable/(Overpayment)		P(52,900,550.67)

Attached to the 1999 4th Quarterly VAT Return is a summary of petitioner's purchases for the period October 1, 1999 up to December 31, 1999 (*Exhibits K-3 and K-4*) as follows:

SUPPLIER	TAXABLE BASE	INPUT VAT
Asiasoft (Phils.) Inc	P 1,239,153.70	P 123,915.37
Philippine Fuji Xerox Corp	40,970.00	4,097.00
THETAN	12,202,490.00	1,220,249.00
Romula Montoya (Rental)	218,181.80	21,818.18
Asian Insights, Inc.	256,263.50	25,626.35
Sithe Philipines Holdings Inc.	32,384,200.00	3,238,420.00
Cunningham Resources	3,560,840.40	356,084.04
Harza	6,307,376.44	630,737.64
Sigma Consulting	1,228,992.40	122,899.24
RW Beck	520,242.65	52,024.27
Designers World Trade Center	2,145.50	214.55
SVA Classic Curtains & Interior	4,545.50	454.55
Cascade Marketing Corp.	3,295.50	329.55
PJES Gen. Mdse.	2,060.90	206.09
Globe Telecom	8,069.70	806.97
DHL Philippines Corp.	52,316.10	5,231.61
Comcore Technologies Corp.	15,895.45	1,589.55
PLDT	81,775.10	8,177.51
Smart Communications Inc.	51,776.30	5,177.63
J & H Marsh & Mclennan	38.40	3.84
Mosaic Communications	6,979.20	697.92
Pacific Office Machines	3,354.50	335.45
Woodward-Clyde Philippines	2,460,812.80	246,081.28
Raytheon Ebasco Overseas	463,140,817.45	46,314,081.75
AGRA Earth	1,249,938.40	124,993.84
Bookhaven, Inc.	32,548.95	3,254.90
Smart Communications Inc.	17,485.89	1,748.59
Western Philippine Corp.	3,398,931.80	339,893.18
Mercan Trading	55,223.80	5,522.38
Jopra Security & Gen. Services	15,939.16	1,593.92

Garden Marketing	142,363.63	14,236.36
Rustan's Mktg Specialists, Inc.	26,318.18	2,631.82
Connect Solutions, Inc.	25,154.55	2,515.46
The Manila Peninsula	220,545.45	22,054.55
Jetour Philippines, Inc.	27,300.00	2,730.00
Being-Lu Marketing, Inc.	1,163.64	116.36
TOTAL[1]		**P52,900,550.67**

Petitioner alleges that the amount of P52,900,550.67 represents excess input VAT paid on its purchases of capital goods and other taxable goods and services. Thus, it filed a claim for refund with the BIR, citing as legal bases the provisions of Section 112(A) and (B) of the NIRC of 1997 quoted earlier.

As clearly shown in petitioner's 4th Quarterly VAT Return for the year 1999, petitioner has no zero-rated sales. Therefore, pursuant to Section 112(A) of the NIRC of 1997, it cannot claim a refund of input VAT on purchases of goods and services attributable to zero-rated sales because said provision presupposes that a sale was actually made ***(Kepco Philippines Corporation vs. The Commissioner of Internal Revenue, CTA Case No. 6413, March 10, 2005; San Roque Power Corporation vs. Commissioner of Internal Revenue, CTA Case No. 6213, December 23, 2004; Kepco Philippines Corporation vs. The Commissioner of Internal Revenue, CTA Case No. 5761, July 14, 2003; Kepco Philippines Corporation vs. The Commissioner of Internal Revenue, CTA Case Nos. 5675 & 5704, March 18, 2003; Placer Dome Technical Services vs. Commissioner of Internal Revenue, CTA Case No. 6106, May 14, 2002; La Frutera vs. Commissioner of Internal Revenue, CTA Case Nos. 5898 and 5937, September 17, 2001)***. Consequently, petitioner's claim for refund shall now be limited to input

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[1] The correct sum is P52,900,550.70

VAT on capital goods pursuant to Section 112(B) of the NIRC of 1997 in relation to the pertinent provisions of Revenue Regulations No. 7-95, *viz*:

Section 4.104-5 of Revenue Regulations No. 7-95 which provides:

> "**SEC. 4.104-5. Substantiation of claims for input tax credit**. — (a) Input taxes shall be allowed only if the domestic purchase of goods, properties or services is made in the course of trade or business. The input tax should be supported by an invoice or receipt showing the information as required under Section 108(a) and 238 of the Code xxx."

Moreover, Section 4.106-1.0 of the same regulation states:

> "**SEC. 4.106-1. Refunds or tax credits of input tax.** — (a) xxx
>
> **(b) Capital Goods** – Only a VAT registered person may apply for issuance of a tax credit certificate or refund of input taxes paid on capital goods imported or locally purchased. The refund shall be allowed to the extent that such input taxes have not been applied against output taxes. The application should be made within two (2) years after the close of the taxable quarter when the importation or purchase was made.
>
> Refund of input taxes on capital goods shall be allowed only to the extent that such capital goods are used in VAT taxable business. If it is also used in exempt operations; the input tax refundable shall only be the ratable portion corresponding to the taxable operations.
>
> *'Capital goods or properties' refer to goods or properties with estimated useful life greater than one year and which are treated as depreciable assets under Section 29 (f), used directly or indirectly in the production or sale of taxable goods or services."*

Thus, based on the law and regulations, in order to be entitled to a refund/tax credit of input VAT paid on capital goods purchased, petitioner must prove that:

1) it is a VAT registered entity;
2) it paid input VAT on capital goods purchased duly supported by VAT invoices or official receipts;
3) it did not offset or apply the claimed input VAT payments on capital goods against any output VAT liability; and
4) the administrative and judicial claims for refund were filed within the two-year prescriptive period ***(Kepco Ilijan Corporation vs.***

The Commissioner of Internal Revenue, CTA Case No. 6324, June 7, 2005).

It bears stressing once more that tax refunds are in the nature of tax exemptions. As such, they are regarded as in derogation of sovereign authority and to be construed in *strictissimi juris* against the person or entity claiming the exemption ***(Commissioner of Internal Revenue vs. Procter and Gamble Phil. Mfg. Corp., 204 SCRA 377; Commissioner of Internal Revenue vs. S.C. Johnson & Son, Inc., 309 SCRA 87).*** Thus, the claimant must be able to establish clearly and convincingly that it has complied with all the above-enumerated requisites in order to be entitled to the refund sought for.

As to the first requisite, petitioner was able to prove that it is a VAT-registered entity as evidenced by the Certificate of Registration issued by the BIR, Revenue District Office No. 06, Urdaneta City *(Annex B)*, in addition to the fact that the same was already stipulated by the parties.

To show compliance with the second requisite, petitioner engaged the services of SGV & Co., pursuant to CTA Circular No. 1-95 as amended by CTA Circular No. 10-97, to validate petitioner's claim for refund/tax credit certificate (TCC) in the amount of P52,900,550.67 representing unutilized input taxes paid on its purchases of capital goods and other taxable goods and services. Based on the report of the commissioned independent CPA *(Exhibit M)*, petitioner was able to substantiate the amount of P50,471,116.54, broken down as follows:

Per Summary List of Purchases			Amount of Input Taxes per SGV Verification				Difference
Exh. No.	**Amount**	**Exhibit No.**	**On Construction Work in Progress**	**On Preoperating Expenses**	**Total**	**Exhibit No.**	
M-1-5	P52,900550.70	M-1-5	P50,304,466.39	P166,650.18	P50,471,116.57	M-1-5	P2,429,434.13
Footing Error	(0.03)				(0.03)		
Net (K-4)	**P52,900,550.67**	**M-1-5**			**P50,471,116.54**	**M-1-5**	**P2,429,434.13**

As per said report, the difference of P2,429,434.13 (P52,900,550.67 – P50,471,116.54) is due to the following reasons:

> "xxx part of the P2,429,434.13 difference above represents input VAT amounting to P1,220,249.00 on domestic purchases of services which are supported by VAT official receipts (ORs) printed before January 1, 1996 and marked with the supplier's TIN 'V' and not with TIN 'VAT'.
>
> The rest of the foregoing difference of P1,209,185.13 represents the input taxes which we were not able to validate. The breakdown of which is as follows:

Item	Nature	Exhibit No.	Amount
1	Input VAT on domestic purchases of services supported by Documents other than VAT official receipts (OR)(supported by acknowledgement receipts)	*M-4*	P23,510.22
2	Input VAT on domestic purchases of services supported by photocopied VAT Ors	*M-5*	59,165.10
3	Input VAT on domestic purchase of service supported by OR with stamped TIN VAT (date of printing not indicated)	*M-6*	454.55
4	Input VAT on domestic purchase of services supported by OR with TAN VAT and not TIN VAT (OR permit to print was dated April 11, 1991	*M-7*	339,893.18
5	Input VAT on domestic purchase of services supported by Ors pre-printed with TIN VAT & Non-VAT	*M-8*	22,054.55
6	Input VAT on domestic purchases of goods supported by Document other than VAT invoices (supported by VAT Ors)	*M-9*	1,063.75
7	Input VAT on domestic purchases of goods supported by photocopied VAT invoices	*M-10*	5,522.38
8	Input VAT on domestic purchase of goods supported by invoice stamped TIN VAT (date of printing not indicated)	*M-11*	206.09
9	Input VAT on domestic purchase of goods supported by invoice with pre-printed VAT Reg TIN (name of the Company not indicated in the invoice)	*M-12*	1,795.45
10	Input VAT on purchases of services supported by VAT Ors not dated within the 4th quarter of 1999	*M-13*	27,244.75

11	Input VAT on payments made to non-residents where the VAT withheld was claimed in the quarter when the payment was made to the non-residents and not in the quarter of the actual Remittance to the BIR, as evidenced by VAT Returns duly filed and paid by the Company on behalf of the said non-residents	*M-14*	707,341.28
12	Purchase of services duly supported by VAT OR but input VAT erroneously computed	*M-15*	0.46
13	Input VAT on purchases of goods supported by VAT invoices not dated within the 4th quarter of 1999	*M-16*	1,929.10
14	Purchases of services paid in foreign currency duly supported by VAT Ors but input VAT was erroneously computed because the foreign exchange rate used does not tally with the prevailing interbank reference rate (IRR)	*M-17*	15,846.33
15	Input VAT on domestic purchases of services without Supporting documents	*M-18*	3,157.94
	TOTAL		P1,209,185.13"

However, a further examination by the Court of the verified amount of P50,471,116.54, reveals that the amount of P166,650.18 representing pre-operating expenses should be likewise disallowed because pre-operating expenses are not subject to depreciation but to amortization. Hence, they cannot be considered capital goods. Although these purchases were supported by valid VAT invoices, petitioner cannot claim for the refund of the input taxes paid pursuant to Section 112(A) of the NIRC of 1997 as earlier discussed.

We shall now limit Our verification on the remaining amount of P50,304,466.39 which represents petitioner's input taxes paid on capital goods.

After a careful review of the various documents presented before this Court, We find that the amount of P250.81 representing input taxes paid on internet services should be disallowed. The said expense cannot be considered as capital goods pursuant to Section 4.106-1 of Revenue Regulations No. 7-95, which defines "capital goods" as "goods with estimated useful life greater than one year and which are treated as depreciable assets under Section 29(f), used directly or indirectly in the production or sale of taxable goods or services".

From the foregoing, input taxes in the total amount of P166,900.99 (P166,650.18 + P250.81) should be denied. Thus, only the aggregate amount of P50,304,215.55 is allowed for being supported by valid VAT official receipts, detailed as follows:

EXHIBITS	SUPPLIER	NATURE OF PURCHASE	REFERENCE	TAXABLE BASE	INPUT VAT
L-13 to L-15	Sithe Philippines Holdings	Construction Mgt Fee	OR 008, 009 & 049	P32,225,736.70	P 3,222,573.67
L-16 to L-17	Cunningham Resources	Consultancy Fee	Bank OR & VAT Declaration	1,432,928.80	143,292.88
L-19 to L-19B	Harza	Management Fee	Bank OR & VAT Declaration	2,867,091.60	286,709.16
L-21 to L-22	Sigma Consulting	Service Fee	Bank OR & VAT Declaration	1,228,992.40	122,899.24
L-23 to L-24	RW Beck	Service Fee	Bank OR & VAT Declaration	172,381.90	17,238.19
L-77 to L-77E	Woodward-Clyde Philippines	Consultancy Fee	OR 2078, 2162	1,881,625.00	188,162.50
L-78 to L-80	Raytheon Ebasco Overseas	Contractor's Fee	OR 18, 19 & 20	46,314,081.75	46,314,081.75
L-81 to L-81B	Agra Earth	Consultancy Fee	Bank OR & VAT Declaration	92,581.90	9,258.19
	Subtotal			P86,215,420.05	P50,304,215.58
	Less: Footing error				0.03
	Total				P50,304,215.55

The above input taxes although paid on purchases of services can be classified as capital goods.

In the case of ***Rohm Apollo Semiconductor Philippines, Inc. vs. Honorable Commissioner of Internal Revenue, CTA Case No. 6534, May 27, 2004***, this Court had the occasion to discuss the cost of services to be within the scope and meaning of the term "capital goods", elucidating that:

> "It has already been settled that the cost of services is within the scope and meaning of the term "capital goods" if the same forms part of the cost of a capital asset. In the case of ***Hopewell Power (Philippines) Corp. vs. Commissioner of Internal Revenue, CTA Case No. 5389, January 4, 1999 [affirmed by the Court of Appeals in the case of Commissioner of Internal Revenue vs. Hopewell Power (Phils.) Corp., CA-G.R. SP No. 51617, March 17, 2001]***, this court ruled that the purchases made by Hopewell consisting mostly of

> engineering and structural services for the construction of its power plant are considered as capital goods. In determining what constitutes capital goods, courts will look to the origin and character of the expenditure to determine whether it is a capital asset. This court found that Hopewell expended for engineering and structural services for the purpose of constructing power plant facilities needed in the production of electricity, which is Hopewell's main product. Thus, it was held that said expenses are necessary and should form part of the cost of the power plant facilities."

Hence, payment for services such as consultancy fee, contractor's fee and construction management fee being necessary for the building of petitioner's power plant can be considered as capital goods.

With regard to the third requisite, there is no doubt that petitioner was able to comply with the same. It did not offset or apply the claimed input VAT payments on capital goods against any output VAT liability. In the 2000 3rd Quarterly VAT Return *(Exhibit J)*, petitioner deducted from the total available input VAT of P212,662,997.40 the amount of P91,549,819.88 *[4th Quarter 1999 P52,900,550.67 + 1st Quarter 2000 P38,649,269.21]*, which includes the amount sought to be refunded *(Exhibit J-3)*.

Lastly, petitioner was able to comply with the fourth requisite. Pursuant to Sections 229 and 112(D) of the NIRC of 1997, petitioner filed the letter claim for refund with the Bureau of Internal Revenue on September 11, 2000 and the present petition for review was filed with this Court on December 26, 2001. Clearly, both were filed within the reglementary period of two (2) years reckoned from January 25, 2000, the date the 4th Quarterly VAT Return for the year 1999 was filed.

In sum, We find petitioner to have sufficiently proven its claim for the refund or issuance of a tax credit certificate representing input VAT paid on the purchases of capital goods, but in the reduced amount of P50,304,215.55, computed as follows:

Amount recommended by the commissioned auditor	P50,471,116.54
Less: Total Disallowances per Court's verification	166,900.99
Amount to be Refunded or to be Issued as Tax Credit Certificate for petitioner	**P50,304,215.55**

WHEREFORE, the instant petition is **PARTIALLY GRANTED**. Accordingly, respondent is hereby **ORDERED** to **REFUND** or **ISSUE A TAX CREDIT CERTIFICATE** in favor of the petitioner in the amount of P50,304,215.55 representing unutilized input VAT paid on its purchases of capital goods for the period October 1 to December 31, 1999.

SO ORDERED.

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Associate Justice

WE CONCUR:

(On leave)
ERLINDA P. UY
Associate Justice

OLGA PALANCA-ENRIQUEZ
Associate Justice

CERTIFICATION

I hereby certify that this Decision was reached after due consultation among the members of this Division in accordance with the provisions of Section 13, Article VIII of the Constitution.

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Chairman