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REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

P.J. KIENER COMPANY, LTD.,
INTERNATIONAL CONSTRUCTION
CORPORATION and GAVINO T.
UNCHUAN,
Petitioners,

- versus - C.T.A. CASE NO. 1224

THE COMMISSIONER OF INTERNAL
REVENUE,
Respondent. 4/13/78

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DECISION

Involved in the instant appeal is the tax exemption provision contained in the Military Bases Agreement between the Republic of the Philippines and the United States of America dated March 14, 1947, and pursued in the "Aide Memoire" between the two Governments on April 27, 1955.

At the outset, it should be stated that during the hearing of this case on September 27, 1973, counsel for petitioners manifested that the issues involved in this appeal are the same as other cases already decided by this Court (notably P.J. Kiener Company, Ltd., International Construction Corporation and Gavino T. Unchuan vs. Commissioner of Internal Revenue, CTA Case No. 1169, June 10, 1965, then pending resolution before the

Supreme Court under G.R. No. L-24754) and suggested that the parties submit a stipulation of facts, to which counsel for respondent agreed.

A "Partial Stipulation of Facts" was, therefore, submitted by the parties, which reads:

The parties, through their respective counsel, to this Honorable Court, respectfully manifest, agree and stipulate as follows:

ON THE ALLEGATIONS COMMON TO ALL CAUSES OF ACTION

1. That the petitioner P.J. Kiener Company, Ltd., is a domestic limited copartnership with offices at No. 319-C Tindalo St., Cebu City, Philippines; petitioner International Construction Corporation is a domestic corporation duly organized and existing under and by virtue of the laws of the Philippines with offices at No. 3111 Magtahan St., Manila, Philippines; and petitioner Gavino T. Unchuan is of legal age, Filipino, a duly licensed Civil Engineer with residence at Cebu City, Philippines. All three (3) petitioners are engaged in the business of contracting, among others;

2. That the respondent, Commissioner of Internal Revenue is an officer of the Republic of the Philippines, empowered, authorized and enjoined by Philippine laws, among other things, to refund taxes illegally and/or erroneously paid and collected or to grant tax credits in lieu thereof;

3. That on or about December 14, 1957, the aforesaid three (3) petitioners entered into a joint venture as contractors for the purpose of bidding for the construction of the Mactan Airfield Project, and if awarded the contract therefor, to undertake jointly the construction of said project;

4. That the Mactan Airfield Project at Mactan Island, Municipality of Opon (now City of Lapu-lapu), Cebu Province, is a project of the Republic of the Philippines represented for this purpose by the Armed Forces of the Philippines which called for a public bidding on January 10, 1958; The funds for the construction thereof are financed by the United States of America inasmuch as the project is intended for the mutual defense of the aforesaid two (2) countries;

5. That having submitted the best bid, petitioners were awarded the job and on February, 1958, the Philippine Republic represented by the Chief of Staff, GHQ, Armed Forces of the Philippines, as Party of the First Part entered into a contract with the petitioners jointly as Parties of the Second Part, Article 1 of which provides:

> "ARTICLE 1. That the advertisement, instructions to bidders, general conditions, Commonwealth Act No. 138, specifications, proposal of the Party of the Second Part and letter of the Chief of Engineers, all of which are hereto attached, together with the plains relating thereto on file in the Office of the Chief of Engineers, GHQ, AFP are hereby made integral parts of this contract by incorporation and reference respectively."

6. That Section 3-19 of the "General Conditions" forming part and parcel of the contract mentioned in the next preceeding paragraph hereof provides as follows:

> "3-19 Taxes - In accordance with the Mutual Defense Agreement between the United States of America and the Republic of the Philippines, no tax of any kind or description will be levied on any material, equipment or supplies which may be purchased or otherwise acquired in connection with

the project under contract, which material equipment or supplies are required solely for such project."

ON THE FIRST CAUSE OF ACTION

7. That during the period from April 30, 1960 thru July 27, 1960, petitioners purchased from Caltex (Phil.) Inc. motor gasoline, kerosene, lubricating or motor oil and diesel fuel oil as shown in the itemized list and statement of the invoice numbers, dates thereof, the commodities purchased and quantitites attached to the original petition as Annex "A" thereof;

8. That under a letter dated March 2, 1961, Caltex filed a claim for tax credit in the sum of P20,107.43 with the office of respondent together with the suppperting documents. (pp. 93-98, Vol. II, BIR Rec.);

9. That this claim has been verified and on July 14, 1961, Revenue Inspector Lorenzo made a favorable recommendation under his memorandum now forming part of Volume II of the BIR Records at Page 103;

10. But Revenue Inspector O. Calsado recommended the reinvestigation of the case as per his memorandum dated August 22, 1961 (p. 107, Vol. II, BIR Rec.);

11. That the petroleum products under the first cause of action of this petition were purchased from the Caltex (Philippines) Inc. in connection with the construction of the Mactan Airfield, Cebu, as per Certificate of Tax Exemption, dated November 28, 1960, with serial number 0409 issued by the Secretary of National Defense thru Col. Eliezer C. Pinto, Chief of Engineer, Armed Forces of the Philippines (pp. 91, 90, 89, 88, 87, Vol. II BIR Records);

12. That upon delivery of the petroleum products mentioned in the preceding paragraph to petitioner at the construction site of the Mactan Airfield, Cebu, the corresponding partial

delivery receipts and invoices issued by Caltex (Phils.), Inc. were stamped on the face of each, "Verified for Tax Exemption" by either Lt. Col. Augusto Roa or Lt. Col. Sergio M. Isada both of the Armed Forces of the Philippines, Project Engineer or Officer-in-Charge, respectively, thru an authorized representative (pp. 2 - 80, BIR Records, Vol. II;

13. That the claim-letter of Caltex (Philippines), Inc., dated March 2, 1961, recorded as File No. 609600-Claim No. DD-573 (p. 98, Vol. II, BIR Rec.) and mentioned in paragraph 8 hereof, is based among others, on the Department of Finance letter, dated July 11, 1958 (p. 93, Vol. II, BIR Rec.) which was attached to said claim-letter of Mr. R.E. Beasly, Manager-Finance & Accounting of Caltex (Philippines), Inc.;

14. That in a letter dated February 21, 1961, petitioner P.J. Kiener submitted, through the Caltex(Philippines), Inc., Certificate of Tax Exemption No. 0409 of the Armed Forces of the Philippines together with the copies of the corresponding partial delivery receipts and invoices of Caltex (Phils.) Inc., covering petroleum products for the months from May to July, 1960 used by petitioners in the construction of Mactan Airfield, Cebu and requested to quote:

> "We respectfully request that you refund to Caltex (Philippines), Inc. the specific taxes or sales taxes paid by it on the petroleum products listed in the accompanying Tax Exemption Certificate at your earliest convenience." (p. 92, Vol. II BIR Record);

15. When the petition for review in this case was filed with this Honorable Court on May 18, 1962, the then Commissioner of Internal Revenue had not as yet acted on the claim; but on January 7, 1963, said

Commissioner denied the same on the ground that the petroleum products purchased by petitioners were not tax-exempt pursuant to a new ruling of the Department of Finance, dated July 14, 1962, as quoted in said letter of denial (p. 117 Vol. II BIR Records);

ON THE SECOND CAUSE OF ACTION

16. The amount claimed under this cause of action is only ₱9[illegible].32 and to the end that this case may be adjudicated at the earliest possible time, petitioners are willing to withdraw this cause of action;

ON THE THIRD CAUSE OF ACTION

17. That during the period from March 6, 1961, through June 12, 1961, petitioners purchased from Caltex (Philippines), Inc. various petroleum products, as shown in the itemized list of the commodities, invoices numbers, dates of purchase, volume of products purchased and quantities attached to the Amended Petition as Annex "E" thereof;

18. That in a letter dated November 10, 1961, petitioner P.J. Kiener Co., Ltd. submitted to respondent through the Caltex (Philippines), Inc. Certificate of Tax Exemption No. 0661 of the Armed Forces of the Philippines, together with copies of the corresponding partial delivery receipts and invoices of Caltex (Philippines), Inc. covering petroleum products of this third cause of action and requested respondent to quote:

> "We respectfully request that you refund to Caltex (Philippines), Inc. the specific taxes or sales taxes paid by it on the petroleum listed in the accompanying Tax Exemption Certificate at your earliest convenience."

19. That as per Certificates of Tax Exemption Nos. 0661 and 0663 of the Armed Forces of the Philippines signed by Col. Paulino Torio, Chief Engineer for the Secretary of National Defense the petroleum products involved in this cause of action were purchased from Caltex (Philippines), Inc. in connection with the construction of the Mactan Airfield, Cebu (pp. 24, 25, and 26, Vol. I, BIR Records);

20. That upon delivery of the petroleum products mentioned in the preceding paragraph to petitioners at the construction site of the Mactan Airfield, Cebu, the corresponding partial delivery receipts and invoices issued by Caltex (Philippines), Inc. were stamped on the face of each, "Verified For Tax Exemption" by Col. Sergio M. Isada of the Armed Forces of the Philippines, Officer-in-Charge of the Mactan Airfield construction thru a duly authorized representative (pp. 8-22, Vol. I, BIR Records);

21. That Caltex (Philippines), Inc. sought from the respondent the tax credit amounting to P1,901.08. Revenue Examiner Gandioso R. Cruel, Jr. under his memorandum dated June 28, 1962 (Page 43, Vol. III, BIR Records) as well as the Chief of the Appellate Division (Page 54, Vol. I, BIR Records) all recommended favorable action on petitioners' claim; but the then Commissioner of Internal Revenue nevertheless denied said claim under his letter dated November 19, 1962 (Page 55, Vol. I, BIR Records) pursuant to the new ruling of the Department of Finance, dated July 18, 1962 quoted therein;

22. That the parties shall introduce evidence in support of their respective position to prove other matters not covered above.

At the scheduled hearing of this case on April 29, 1977, after the trial was postponed for several times upon request of the parties, counsel for petitioners manifested that respondent intends to file, within thirty (30) days, a motion to dismiss, together with his memorandum in support thereof. The Court thus granted petitioners a period of thirty (30) days from receipt of respondent's memorandum within which to file their memorandum in answer thereto. No trial on the merits was, therefore, conducted by the Court.

After several extensions of time, respondent finally submitted his memorandum on Decembér 29, 1977, and because petitioners failed to file their memorandum within the time granted by the Court, the case was considered submitted for decision as of February 2 , 1978.

The decisive issue involved in this case boils down to the determination of whether the petroleum products in question are "materials" or "supplies" purchased or otherwise acquired in connection with the construction of the Mactan Airfield and as such, were required "solely" for said project and, therefore, covered by the tax-exemption provision of the Mutual Defense Agreement between the Philippines and the United States of America.

Four-square with the case at bar on this point, by reason of the exact identity of the parties, the issue litigated, and the tax-exemption provision in the Military Bases Agreement between the Philippines and the United States as pursued in the "Aide Memoire" involved herein, including the factual setting of the case, is Commissioner of Internal Revenue vs. P.J. Kiener Company, Ltd., International Construction Corporation, Gavino T. Unchuan and Court of Tax Appeals, L-24754, July 18, 1975, 65 SCRA 142.

In that case, the Supreme Court disposed of the same question before us in clear and unequivocal terms, in the following wise:

> "Explicitly, the "materials" and "supplies" must be for exclusive use in, in connection with, and required solely for the construction of the Mactan Airfield. In short, the "materials" and "supplies" need be incorporated in the construction for the exemption to apply."

Because the conclusion reached by the Supreme Court in the above-cited case should resolve once and for all the identical problem now brought before us by the same parties in this proceeding, we will quote the following rationale of the decision:

Private respondents (petitioners herein) flawlesaly narrate that when they began construction towards the middle of 1958, they started purchasing the petroleum products from Caltex (Phil.) Inc. "to run and maintain their machineries and equipment used in the construction." The "equipment" fefers to fuel pumping machineries, radar facilities, and the like. Purchase went through April 11, 1960, when months thereafter the conflict on the tax credit arose. Private respondents would deliver the conclusion that these petroleum products are tax-exempt since they have been " . . . . . purchased or otherwise acquired in connection with the project. . . " The fact that they are not incorporated into the Mactan Airbase would not defeat the exemption.

The sense which private respondents (petitioner herein) proffer to attach to the terms "materials" and "supplies" eludes the link welded into the Military Bases Agreement and "Aide Memoire" and recognized in Section 3-19 of the "General Conditions". The Military Bases Agreement states that "No import, excise, consumption or other tax . . . shall be charged on material, equipment, supplies or goods, . . . for exclusive use in the construction . . . . of the bases . . . " (Art. V, footnote 1). The "Aide Memoire" provides: " . . . no internal taxes of any kind or description, except income taxes, shall be levied on any materials, equipment, supplies and/or services which may be purchased or otherwise acquired in connection with the /construction of the Mactan Airfield/ . . . " (Sec. 6, Footnote 2). Section 13-9 of the "General Condition" stipulates that " . . . no tax of any kind or description will be levied on any material, equipment or supplies which may be purchased or otherwise acquired in connection with the project . . . ." Reduced into simple terms, the underscored phrases continuously used in the two treaties and in the contract could only mean, collectively, "construction" materials or supplies which must necessarily be incorporated in the construction of the airfield. For the terms "materials" and "supplies" refer to something "going into or consumed" in the performance of the work such as mortar, cement, sand, bricks, lumber or nails, glass, hardware, and a thousand other things that might be meant, which are necessary to the completed erection of a building or structure.

Thus examined, the petroleum products purchased by the private respondents "to run and maintain their machineries and equipment" cannot be categorized as "materials" or "supplies" since they do not go into or are consumed in the construction, but in the machineries and equipment.

Nonetheless, private respondents (petitioners herein) would unwrap a thesis that if Section 13-9 of the "General Conditions" intended to refer only to "materials" or "supplies" which form part and/or incorporated into the project, the said section would have so stated, just like when it provided that "Only equipment which will be incorporated in the construction" are tax free. They would thus seize the absence of such proviso as a recognition of the tax-exemption of those "materials" or "supplies" not necessarily incorporated in the construction. The argument misses the point. In its textual completeness, Section 13-9 provides: "Only equipment which will be incorporated in the construction can be imported tax free on certification of the Engineer". (Last sentence, 2nd par.) It deals centrally on the importation of equipment. The Government had conceded the privilege of exemption to this item because the same may not be "economically procurable in terms of price and quality within the Philippines." (Sec. 2, "Aide Memoire"). To assure, however, that the privilege is not abused or circumvented, the Government has stipulated in Section 13-9 of the "General Conditions" that the equipment "[must] be incorporated in the construction . . . ." It was intended by the Government as an open restraint against possible detour of the revenue and customs laws. The reason is easily discernible. There still pervaded even at that time the sentiment of preference to local products, as can be plucked from the ultimate sentence of Section 2, "Aide Memoire", thus:

> "Locally produced materials, however, shall be used wherever such materials are of satisfactory quality and are available at reasonable, comparable prices."

> Under these circumstances, the contractual proviso in Section 13-9 (supra) cannot be isolated and stretched to mean that "materials" and "supplies" need not be incorporated in the construction to be tax-exempt. It is essential non sequitur.

Accordingly, we find no merit in this petition for review filed by P.J. Kiener Company, Ltd., International Construction Corporation and Gavino T. Unchuan. The decisions of respondent Commissioner of Internal Revenue denying petitioners' claims for refund and/or tax credit involved in this case are, therefore, affirmed.

WHEREFORE, the instant appeal is hereby dismissed at petitioners' cost.

SO ORDERED.

Quezon City, April 13, 1978.

Amante Filler
AMANTE FILLER
Acting Presiding Judge

I CONCUR:

CONSTANTE C. ROAQUIN
Associate Judge