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REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

CARLSBERG PHILIPPINES, INC.,
Petitioner,

- versus -

C.T.A. CASE NO. 4712

COMMISSIONER OF INTERNAL REVENUE,
Respondent.
x - - - - - - - - - - - - x

7/5/93

D E C I S I O N

Having admitted the material allegations of the petitioner and there being no objection on the part of the respondent, this Court hereby resolves to grant petitioner's motion for judgment on the pleadings.

Petitioner is a trader engaged in the business of buying locally manufactured beer for the purpose of reselling them in their original state. Being among those that were subjected to the Value-Added Tax (VAT) it availed of the 8% presumptive input tax under Sec. 25 of Executive Order 273 (E.O. 273).

The petitioner applied the 8% presumptive input tax on its inventories including on those goods for resale as of December 31, 1987 consisting of beer with a total value of P7,640,969.64.

However, the respondent, claiming that the petitioner is not covered by Sec. 25 of EO 273, made an assessment for VAT deficiency in the total amount of P1,429,647.17 inclusive of the disallowance of the presumptive input on its inventory of supplies and penalties.

The only issue to be resolved in this case is whether or not the petitioner can avail of the 8% presumptive input tax under Sec. 25(3) of EO 273 on its inventory of beer valued at P7,640,969.64.

We rule in favor of the petitioner.

Section 25 of Executive Order No. 273 provides:

> "SEC. 25 - Transitory provisions.- (a) All VAT-registered person shall be allowed transitional input taxes which can be credited against output tax in the same manner as provided in Section 104 of the National Internal Revenue Code as follows:
>
> > 1.) xxx xxx xxx
> > 2.) xxx xxx xxx
> > 3.) A presumptive input tax equivalent to 8% of the value of the inventory as of December 31, 1987 of goods for sale, the tax on which was not taken up or claimed as deferred sales tax credit."

The respondent interpreted "goods for sale" under Sec. 25(3) as limited to those referred to in Sec. 166 of the former Tax Code, which provides:

> "SEC. 166. Tax Credit. - (a) Creditable Taxes. - Any excise, sales or miller's tax paid under this Title and Tile V of this Code on domestically manufactured, processed, produced or imported raw materials, part, accessory or other article locally purchased or imported by the manufacturer for conversion into or intended to form part of any finished product for sale shall be credited against the sales tax on the original sale of the finished product, except agricultural products: Provided, however, That the amount of sales tax on domestically purchased raw material, part or accessory, is separately indicated in the sales invoice.

The respondent maintains that to be able to avail of the 8% presumptive input tax under Sec. 25(3) of EO 273, the inventory of goods referred to therein must consist of raw materials or articles that would be converted into or would form part of a finished product.

Thus, the respondent rejected the petitioner's claim for a presumptive input tax on its inventory of beer "because beer is not used as a raw material of a finished product subject to sales tax." (Annex "L" of Petition)

It is a fundamental and basic precept of statutory construction that in interpreting the meaning and scope of a term as used in a law, a careful review of the whole law involved must be made, looking likewise into the intendment of the law (Chan Rung Fa vs. Gianzon, 97 Phil 913).

One need not go beyond Sec. 25 above-quoted to be able to conclude that the phrase "the tax on which was not taken up or claimed as deferred sales tax credit" is not intended to restrictly qualify the subject inventory to those articles mentioned under Sec. 166 of the former Tax Code. Sec. 25(2) which is similarly qualified by the said phrase provides:

> "xxx xxx xxx
>
> 2.) A presumptive input tax equivalent to 8% of the value of the inventory as of December 31, 1987 of <u>materials and supplies which are not for sale, the tax on which was not taken up or claimed as deferred sales tax credit</u>; (Underscoring supplied)
>
> xxx xxx xxx."

The inventory of "materials and supplies" abovementioned could not possibly contemplate the "raw materials of a finished product" inasmuch as they are not intended for further processing and are being used in business in their present condition. Machinery parts and equipment not falling under the definition of "capital goods" may come within the purview of the term "supplies". The respondent even admits in his VAT ruling (Annex

"D" of the petition) that an inventory of supplies consisting of bottles may be subject of the 8% presumptive input tax under Sec. 25(2) and which article, like beer, is definitely not "a raw material of a finished product subject to sales tax".

Thus, no less than the respondent had made the admission that the last phrase appearing in both 2 and 3 of Sec. 25 does not restrict the subject inventories to the articles mentioned in Sec. 166 of the former Tax Code. It merely excludes from its application those goods and supplies whose taxes were already claimed as deferred sales tax credit.

Sec. 105 of the National Internal Revenue Code as added by EO 273 provides:

> "Sec. 105. Transitional Input Tax. - A person who becomes liable to value-added tax or any person who elects to be a VAT-registered person shall subject to the filing of an inventory as prescribed by regulations, be allowed input tax on his beginning inventory of goods, materials and supplies equivalent to 8% of the value of such inventory or the actual value added tax paid on such goods, materials, and supplies, whichever is higher which shall be creditable against the output tax."

Note that under this provision, the 8% presumptive input tax is made to apply generally to the goods, materials and supplies of persons who become liable to VAT or who elects to become VAT-registered without the exception appearing under Sec. 25 (2) and (3).

Consequently, those who similarly engage in the business of the petitioner (trader of beer) whose annual gross sales does not exceed P200,000.00 but who elects to register under VAT and those whose annual gross sales shall exceed P200,000.00 are entitled to the 8% presumptive input (or actual VAT paid) under Sec. 105 in conjunction with Sec. 17 of the implementing rules and regulations (Revenue Regulation 5-87) regardless of whether the tax on such goods had been claimed as deferred sales tax credit under Sec. 166 of the former Tax Code.

The VAT embodied in EO 273 which took effect on January 1, 1988 imposes a uniform rate covering all persons engaged in the business of selling goods and services which not only applies to manufacturers, producers, and importers, but subsequent sellers as well, including wholesale distributors, traders, and retailers. Under this present system not only original sellers but also subsequent sellers are entitled to claim tax credit.

The framers of EO 273 must have been fully aware of the initially persistent criticisms and misapprehensions over the proposed tax reform as typified in those issued raised in the case of **KMU** vs. Executive Secretary (163 SCRA 371), particularly, the fear of price increase. They must have also known that due to its enlarged scope, different sellers then subject to different tax rates would suddenly be charged with a constant tax rate of 10%, unless zero-rated. Consequently, a trader who, at the time of the law's conception, is paying the lower 1.5% turnover tax, would eventually be subjected to an abrupt 8.5% increase in its tax liability for its inventory of goods existing by the end of December 1987 subsequently sold. Being an indirect tax, it may very well be expected that the additional tax burden will ultimately be passed on to the buying public or consumers in the form of unpopular price increase.

Such a scenario is further enhanced by the unavoidable situation on the initial implementation of the VAT - the lack of a valid or actual VAT input on the sellers' stock of goods bought before January 1, 1988 inasmuch as they were never subjected to 10% VAT.

While manufacturers, producers and importers covered by the old sales tax law may legally avail of a last tax credit under Sec. 166 of the former Tax Code, subsequent sellers not covered by said provision may not, although under EO 273, they are supposed to be placed on equal footing with the original sellers by similarly being entitled to claim a tax credit on purchases of raw materials, supplies, capital equipment and services made in the course of their trade or business. This situation, impugns the characteristically uniform and equitable nature of the VAT. It is in this light that the transitory provision of EO 273 should be interpreted.

The 8% presumptive input seeks to remedy or at least alleviate the iniquitous situations which would necessarily arise during the transition from the old to the new tax law. It also seeks to put in check any possibility of price destabilization, and ensure a uniform and equitable application of the law. In other words, the provision was incorporated under EO 273 to pave the way for a smooth transition into the new tax law.

The foregoing discussion elucidates petitioner's argument that Sec. 25 should generally apply to every VAT-registrant. It is, in fact, in harmony with the very provision itself when it stated:

> Sec. 25. Transitory provisions. - (a) All VAT-registered persons shall be allowed transitional input taxes which can be credited against output tax in the same manner as provided in Sec. 104 of the National Internal Revenue Code as follows:
>
> xxx xxx xxx."
> (Underscoring supplied)

The phrase "the tax on which was not taken up or claimed as deferred sales tax credit does not qualify the phrase "All-VAT-registrants" which include petitioner herein but "goods for sale". However, it simply means that any VAT-registrant may avail of the 8% presumptive tax on its inventory as of December 31, 1987 over goods on which it has not availed of, or cannot avail of the tax credit under Sec. 166.

This construction eradicates the inequity of denying other VAT taxpayer from being able to avail of a tax credit in its first payment of VAT.

The respondent, in its answer laid stress "that the transitory provision in the aforestated EO 273 simply provides for the mechanics of adjustment from one tax system to another. Thus, if tax crediting by a trader of a finished product (subject to turnover tax) is not allowed, it cannot, similarly, be claimed as presumptive input tax credit under the VAT system (EO 273)".

This constricted view on the function of a transitory provision had likewise led to the limited interpretation of Sec. 25 of EO 273. It suffices to state that transitory or temporary provisions are frequently necessary to provide for special situations in the transition period and the establishment of the new law (Sutherland Statutory Construction, 4th Ed. Vol. 1A 20.21).

WHEREFORE, judgment is hereby rendered allowing the 8% presumptive input on petitioner's inventory of goods valued at P7,640,969,64 and accordingly, hereby orders the cancellation of the deficiency VAT assessment in the amount of P1,429,647.17 covered by Assessment Notice and Letter of Demand No. FAS-4-88-91001057 dated March 30, 1991.

SO ORDERED.

Quezon City Metro Manila, July 5, 1993.

ERNESTO D. ACOSTA
Presiding Judge

WE CONCUR:

MANUEL K. GRUBA
Associate Judge

RAMON O. DE VEYRA
Associate Judge

CERTIFICATION

I hereby certify that this decision was reached after due consultation among the members of the Court of Tax Appeals in accordance with Section 13, Article VIII of the **Constitution.**

ERNESTO D. ACOSTA
Presiding Judge
Court of Tax Appeals