REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

PHILIPPINE PHOSPHATE FERTILIZER CORPORATION,
Petitioner,

-versus - C.T.A. CASE NO. 4661

THE HONORABLE COMMISSIONER OF CUSTOMS,
Respondent.

5/31/93

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D E C I S I O N

This is a petition for review instituted by Petitioner from the denial by Respondent of its claim for refund amounting to a total of P14,362,309 representing customs duties paid on petroleum products delivered to it by Petrophil Corporation (PETRON) for the period January 1987 to December 1990.

It appears from the records of the case that Philippine Phosphate Fertilizer Corporation (Philphos) is a domestic corporation engaged in the business of manufacturing fertilizers for domestic and international distribution. It is a registered

Export Processing Zone enterprise under Presidential Decree No. 66, as amended. As part of its operational needs, it has to procure from local oil companies like Petron its fuel requirements like diesel, fuel oil and lubricant. In the sale of petroleum products to Philphos, customs duties and ad valorem taxes are passed on by Petron. Philphos believing that it is exempted from customs duties and taxes on its purchase of fuel and other petroleum products filed a claim for refund of the corresponding duties passed on to it by Petron. The first claim was made under its letter dated October 22, 1990 in the amount of P4,766,833.43 covering the period from January 1989 to June 1990. This claim was denied by the Commissioner of Customs in a letter, dated 26 November 1990, received by Petitioner on December 26, 1990.

Again on August 21, 1991, Petitioner, through counsel, reiterated various claims for refund covering the period from January 1988 to December of 1990. This claim was likewise denied by the Respondent under his letter, dated September 13, 1991, received by Petitioner's counsel on September 26, 1991. This denial was in turn based on the 2nd

Indorsement, dated August 23, 1991, of the Acting Secretary of Finance denying the request for reconsideration by Philphos of the decision of the Respondent Commissioner.

From this latter decision of the Respondent, Petitioner instituted the instant Petition for Review filed with this Court on October 26, 1991.

From the memorandum of the Petitioner, it appears that the following claims are involved in this case:

1. P2,184,251.01 representing customs duties passed on to Philphos from January to December 1987;

2. P1,584,928.00 representing customs duties passed on to Philphos from January to December 1988;

3. P4,766,833.43 representing customs duties passed on to Philphos from January 1989 to June 1990;

4. P1,698,724.64 representing customs duties passed on to Philphos from July to December 1990;

5. P4,147,572.13 representing customs duties passed on to Philphos from January to May 1991.

The aforementioned facts were admitted by Respondent in his answer including the various amount of the refund claimed and although contained only in the memorandum of the Petitioner remains uncontroverted. Instead, Respondent concentrated to dispute the legal basis of the request for refund.

Petitioner on its part, alleged that it is entitled to the refund being claimed pursuant to Section 17 of the Presidential Decree No. 66, or the EPZA Law, also citing a previous ruling of the Secretary of Finance on the matter. Petitioner advanced the concept of the Export Processing Zone as a foreign territory for customs purposes, for which reason, when merchandise is brought into the zone, no Philippine tax may be imposed. It also cited Letter of Instruction No. 942, dated October 16, 1979 and paragraph 2 of Article 17 of Executive Order No. 226, considering merchandise brought to the zone as "export sale".

Respondent on his part alleged that Section 17 of PD 66 does not apply in this particular case and that the cited opinion of Secretary Alfredo Pio de Roda has already been superseded by subsequent rulings of the Secretary of Finance. He cited instead Section 18(1) of PD 66, as amended by PD 1449, which allows refunds through tax credit of duties and taxes on supplies only if the supplies utilized in the manufacture, processing or production of export products form part of the finished products exported. On the argument concerning the application of constructive export under the cited LOI and Executive Order, Respondent argues that the same would apply only to merchandise which will later form part of the finished products for export citing Section 127(d) of the Tax Code requiring actual exportation of product. Granting that this sale of petroleum products to zone enterprise meant tax refund, the same should accrue to the seller.

Considering the foregoing allegations of the parties, the issue submitted for resolution of this Court is whether or not deliveries by local oil companies of petroleum products to an export processing zone enterprise may not be subject to customs duties.

We quote hereunder the pertinent provisions of Section 17(1) and Section 18(i) of Presidential Decree No. 66 as amended by P.D. No. 1449:

P.D. No. 66
Nov. 20, 1972

Creating the Export Processing Zone
Authority And Revising
Republic Act No. 5490

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Sec. 17. *Tax Treatment of Merchandise in the Zone.* - (1) Except as otherwise provided in this Decree, foreign and domestic merchandise, raw materials, supplies, articles, equipment, machineries, spare parts and wares of every description, except those prohibited by law, brought into the Zone to be sold, stored, broken up, repacked, assembled, installed, sorted, cleaned, graded, or otherwise processed, manipulated, manufactured, mixed with foreign or domestic merchandise or used whether directly or indirectly in such activity, shall not be subject to customs and internal revenue laws and regulations nor to local tax ordinances, the provisions of law to the contrary notwithstanding.

(2) Merchandise purchased by a registered zone enterprise from the customs territory, if paid for in the United States dollar or in any

> convertible foreign currency and subsequently brought into the zone, shall be considered as exported, and the exporter thereof shall be entitled to the benefits allowed by law for such transaction.
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> Sec. 18. *Additional Incentive.* - A zone registered enterprise shall also enjoy the following incentives and benefits xxx:
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> (i) Tax credit. Every registered zone enterprise shall enjoy tax credit equivalent to sales, compensating and specific taxes and duties on supplies, raw materials and semi-manufactured products used in the manufacture, processing or production of its export products and forming part thereof: Provided, that the tax credit shall accrue to the registered zone enterprise only after the final product has in fact been exported xxx"

Before going into the specific interpretation of the above provisions of law, we believe a narration of the background, objectives and policies will assist this Court in arriving at a better construction of the aforequoted provisions of law.

The Export Processing Zone was an original creation of Republic Act No. 5490 on June 21, 1969. It created a foreign trade zone in the Port of Mariveles and has declared the following policy as reason for its creation:

R.A. No. 5490

An Act Making Mariveles, Province of Bataan, a Port of Entry by Amending Section Seven Hundred one of the Tariff and Customs Code of the Philippines. As Amended, Providing For the Establishment, Operation and Maintenance of a Foreign Trade Zone Therein; Creating a Foreign Trade Zone Authority; And Authorizing The Appropriation of the Necessary Funds Therefor.

> Section 1. *Declaration of Policy.* - It is hereby to be the policy of the government to stimulate, expedite, encourage and promote foreign commerce as a means of making the Philippines a vital center of international trade, of strengthening our foreign exchange position, of hastening industrialization, of overcoming domestic unemployment, of accelerating the development of the country and of insuring the economic security of all the people as provided in the Constitution.

To attain said objectives, the law amended section 701 of the Tariff and Customs Code and provides as follows:

> "Sec. 701. *Collection Districts and Ports of Entry Thereof.* -
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> xxx xxx xxx

> There is hereby established in the Mariveles Port a foreign trade zone herein referred to as the Zone. Foreign and domestic merchandise of every description except such as is prohibited by law, may, without being , subject to the customs and internal revenue laws and regulations of the Philippines, except as otherwise provided in this Act, be brought into the Zone and may be stored, sold, exhibited, broken up, repacked, assembled, distributed, sorted, graded, cleaned, mixed with foreign or domestic merchandise, or otherwise manipulated, or be manufactured except as otherwise provided in this Act, and be exported, destroyed or sent into customs territory of the Philippines therefrom, in the original package or otherwise, under the following terms and conditions:

Republic Act No. 5490 failed to mention as an incentive the grant of tax credit for raw materials utilized in the manufacture of finished products exported. This law was substantially amended by Presidential Decree No. 66 on November 20, 1972, renaming the foreign trade zone as an export processing zone. Thus the latter law expanded the operation of the zone by authorizing the opening of more export processing zone in other parts of the country. The same policies and objectives were likewise recited in this latter law. The presidential decree expanded the incentives that a zone enterprise may enjoy under the law. It provides the incentive under Section 17(1)(2) aforequoted which is similar to the incentive provided under Section 701 of the Tariff and Customs Code as amended by said Republic Act No. 5490.

Subsequently, Presidential Decree No. 1449 was issued on June 11, 1978 introducing several amendments to Presidential Decree No. 66. Among others, it amended Section 18 by adding new paragraphs one of which is the aforequoted Section 18(i) which grants tax credit to every registered zone enterprise equivalent to the sales, compensating and specific taxes and duties on supplies & raw materials used in the manufacture of products exported and forming part thereof. P.D. 1449 did not touch on Section 17 of P.D. 66.

However, on October 16, 1979, Letter of Instruction No. 942 was issued by the President which provides among others that:

xxx xxx xxx

"7. Sales and delivery of products to bonded warehouse of export-oriented manufacturers and to export processing

> zone enterprises can be considered as "export sales" and products constructively exported, so that tax credit and duty drawback can be availed of immediately, without awaiting for actual exportation of the finished products abroad. For this purposes, the requirement that the exporter has in fact exported shall include constructive exportation as above defined."

Lately, the EPZA law was again amended by Executive Order No. 226, otherwise known as the Omnibus Investment Code of 1987. Section 17(1) & (2) aforequoted was retained with a little modification of the latter subsection. The requirement on the foreign exchange payment for merchandise was deleted. Thus, the provision reads as follows:

E.O. No. 226

The Omnibus Investment Code of 1987

> ART. 77. *Tax Treatment of Merchandise in the Zone.* - (1) Except as otherwise provided in this Code, foreign and domestic merchandise, raw materials, supplies, articles, equipment, machineries, spare parts and wares of every description, except those prohibited by law, brought into the zone to be sold, stored, broken up, repacked, assembled, installed, sorted, cleaned, graded, or otherwise processed, manipulated, manufactured, mixed wiith foreign or domestic merchandise whether directly or indirectly related in such

> activiy, shall not be subject to customs and internal revenue laws and regulations nor to local tax ordinances, the provision of law to the contrary notwithstanding.
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> (2) Merchandise purchased by a registered zone enterprise from the customs territory and subsequently brought into the zone, shall be considered as export sales and the exporter shall be entitled to the benefits allowed by law for such transaction.

The aforequoted provisions of law and other incentives for export processing zone enterprise are all incorporated under Book VI of the said Executive Order. In the incorporation the previous Section 18(i) of P.D. 66 as amended by P.D. 1449 was not reproduced under this Book but was merely referred by Article 78 as one the additional incentives, an EPZA registered enterprise may be entitled under Article 39. The incentives referred to under Article 39 are those that are normally enjoyed by BOI registered enterprises.

We can see that from the above presentation of the laws involved, the provision of Section 17(1) is maintained as a principal incentive or source of incentives. It has never been deleted from the provision of the EPZA law. Unlike Section 18(i) which may have been inserted by P.D. 1449 as an additional incentive thinking that it will serve as an additional attraction to zone enterprises.

A close analysis of the said Section 17(1)(2) will show that it allows foreign or domestic merchandise, raw materials and supplies, except those prohibited by law to be brought into the zone for sale, storage, repacking, processing, manufacturing, mixed with foreign or domestic merchandise or used whether directly or indirectly in such activity and shall not be subject to customs and internal revenue laws and regulations nor to local tax ordinances. This privilege will be enjoyed notwithstanding the provision of other law to the contrary.

Contrary to the allegation of the Respondent that Section 17(1) does not provide for duty and tax exemption privilege, this Court disagrees. The phrase "shall not be subject to customs and internal revenue laws and regulations nor to local tax ordinances, the provisions of law to the contrary notwithstanding" cannot be interpreted in any other manner than to mean that merchandise or supplies brought into the zone are exempt from customs duties and taxes. The incentive given under Section 17(1) is broader than a mere tax exemption. The phrase is so broad to include not only the exemption from customs duties and taxes but everything required in the enforcement of the customs and internal revenue laws save on the exceptions and conditions specified in the EPZA law itself. Considering that the customs and internal revenue laws are primarily enacted to impose duties and taxes, the phrase cannot be interpreted to exclude these impositions. More so, the phrase will also include exemption from other rules and regulations which are normally followed in the discharge of importation such as the filing of import entries, examination and appraisal of goods by customs authorities and other requirements attendant to the importation of goods into the country.

In fact, contrary to the allegation of Respondent, said Section 17(1) is cited by the Export Processing Zone Authority as source of tax exemption privileges in the issuance of its implementing rules and regulations. Thus Section 1 of Rule IV of the "Amended Rules and Regulations to Implement Presidential Decree No. 66, as Further Amended by Executive Order No. 226 Otherwise Known as the Omnibus Investments Code of 1987" mentions "exemption" citing paragraph 1, Article 77 (Sec. 17 under P.D. 66) of the Code. Likewise, Section 1(B) Rule VIII grants tax credit on domestic capital equipment, Section 3 of the same Rule grants exemption from Value Added Tax on local purchase, Section 1 of Rule IX on tax and duty exemption of the importation of capital equipment and Section 2 of said Rule IX allows the tax and duty free importation of construction materials, all cited Article 77(1) as source of legal basis. Unfortunately, the said implementing regulation fails to cover all possible situations that may occur in its implementation. One situation is the tax treatment of petroleum products supplied by local oil companies to an export processing zone registered enterprise. This as the subject of the dispute between the Petitioner and Respondent which this Court is called upon to interpret.

Section 17(1) covers domestic merchandise, raw materials, supplies, articles and wares of every description, except those prohibited by law, brought into the zone to be sold, stored, broken up, repacked, assembled, installed, sorted, cleaned, graded or otherwise processed, manipulated, manufactured, mixed or used directly or indirectly in such activity shall not be subject to customs and internal revenue laws and regulations. Oil products produced by local oil companies may be classified as domestic merchandise, raw materials or supplies as legally defined in the Supreme Court case of Commissioner of Customs vs. Caltex (Philippines), Inc. (GR No. L-13067, Dec. 29, 1959, 106 Phil 829) which states that supplies or materials shall include gasoline and other petroleum products for purposes of exemption from customs duties under Article 103 of Republic No. 387. For what purpose, among others, these products may be brought into the zone for processing, manipulation, manufacture, mixed with foreign and domestic merchandise or used directly or indirectly in such activity. In our particular case, the petroleum products delivered to Petitioner is used in the processing of fertilizer for export. While Respondent may be correct that these products did not form part of the fertilizer exported nevertheless, the law does not provide for such requirement but only requires the use of such materials directly or indirectly in such activity. The use of petroleum products like bunker oil as fuel will easily fall under the phrase "used directly or indirectly in such activity". Clearly these petroleum products can easily qualify for tax and duty free privileges under Section 17(1) of P.D. 66.

Regarding the allegation of the Respondent that Section 18(i) shall govern the situation and therefore the claim for refund of customs duties should be denied as the bunker oil used as fuel did not actually form part of the finished product exported. This Court believes that this section introduced by P.D. 1449 merely grants additional incentive to an EPZA registered enterprise and was not meant to supersede Section 17 of P.D. 66. This is clear as the heading clearly indicates that it is an "additional incentive". The grantee of the incentive may or may not avail itself of it. In fact, this Court would interpret that this incentive as a surplusage. Its provision was not intended to restrict the enjoyment of the privileges under Section 17, otherwise the amending law, P.D. 1449, should have stated so. On the contrary it was meant only as an incentive in addition to those already being enjoyed by an EPZA registered enterprise.

This interpretation is strengthened by the enactment of E.O. 226 (The Omnibus Investments Code). The tax treatment of merchandise inside the zone was re-enacted under Article 77 of Book VI of the Code but not Section 18(i). Said Section 18(i) was deleted from book VI governing incentives of EPZA registered enterprise and was incorporated as one of the incentives of a BOI registered enterprise under Book I which an EPZA registered enterprise may also enjoy as an additional incentive under Art. 78.

Furthermore, under paragraph (2) of said Section 17, merchandise purchased by a registered zone enterprise from the customs territory, if paid for in foreign currency and subsequently brought into the zone shall be considered as exported and the exporter shall be entitled to the benefits allowed by law for such transaction. This provision was reiterated with modification under Letter of Instruction No. 942 issued on October 16, 1979 which provides as follows:

> "7. Sales and delivery of products to bonded warehouse of export-oriented manufacturers and to export processing zone enterprises can be considered as "export sales" and products constructively exported, so that tax credit and duty drawback can be availed of immediately, without awaiting for actual exportation of the finished products abroad. For this purposes, the requirement that the exporter has in fact exported shall include constructive exportation as above defined."

Finally under paragraph (2) of E.O. 226 aforequoted, the purchase of merchandise by a registered zone enterprise was likewise considered as export sale and the exporter shall be entitled to the benefits allowed by law for such transaction. This will entitle the exporter to duty drawback under Section 106 of the Tariff and Customs Code and tax credit under Section 127(d) of the National Internal Revenue Code. Considering that pursuant to the aforequoted provision of the LOI and E.O. 226, the mere act of selling and delivering products to the export processing zone enterprise can be considered already as export sale without awaiting for actual exportation, the allegation of the Respondent that the article sold to an EPZA registered enterprise should form part of the finished product actually exported will hold no water at all.

All the above incentives spring from the concept that an export processing zone is carved out of the Philippine territory for purposes of enforcement of customs and tax laws. So that the area or areas fixed or delimited by presidential proclamation or by board resolution of the Export Processing Zone Authority as export processing zone shall be referred to as the "zone" and the national territory outside of the zone shall be called "customs territory" (Section 2(e) & (f) of the Amended Rules and Regulations to Implement P.D. 66). The basic policy in establishing a zone is to attract enterprises especially foreign investors who will be manufacturing products primarily for export and be able to do so without their supplies and raw materials entering, and the export products leaving the Philippine territory within the context of customs and revenue regulations. Export is the backbone of our economy and is being encouraged by providing enterprises with all the incentives including those which we have discussed above. For which reason the law further states that "All doubts concerning the benefits and incentives granted enterprises and investors by the Code shall be resolved in favor of investors and registered enterprises". (Article 79 E.O. 226.)

In view of all the foregoing, this Court holds that bunker fuel oil and other oil products sold and delivered by local oil companies to an EPZA registered enterprise shall be exempted from customs duties and internal revenue taxes and if said duties and taxes were passed on by the supplier to the EPZA registered enterprise duty drawback and tax credit shall be granted to the latter pursuant to the provisions of Section 17(1)(2) of P.D. 66 as amended under Article 77(1)(2) of E.O. 226.

However, from the records of this case the following facts are very apparent:

(1) The P2,164,251.01 claim representing customs duties allegedly paid by Philphos for the period January to December 1987 should be denied for want of a valid claim for refund. Petitioner never filed a claim for refund covering this amount with the Commissioner of Customs. Hence, there can be no valid decision of the Commissioner of Customs to appeal from;

(2) The same is true with regard to the amount of P4,147,572.13 representing customs duties allegedly paid for the period January to May 1991. There was neither a claim for refund filed nor a decision by the Commissioner of Customs;

(3) The amount of P4,766,833.43 representing customs duties allegedly paid by Philphos for the period January 1989 to June 1990 should also be denied for failure of the Petitioner to appeal on time from the decision of the Commissioner denying said claim. The records show that the claim was

denied by the Respondent in a letter, dated November 26, 1990, and received by Petitioner on December 26, 1990. No appeal or petition for review was ever filed from said denial within the 30-day period.

In all the above instances, this Court has to dismiss the said claims for refund for lack of jurisdiction.

The remaining valid claims are those covered by the letter, dated August 21, 1991, of the counsel of Petitioner covering the period from January to December 1988 in the amount of P1,584,928.00 and from July 1990 to December 1990 in the amount of P1,698,724.64. Of the amount covered by these two claims, only the following amounts were substantiated by the Petitioner with evidence:

(1) P166,989.06 covering customs duties paid for the month of JUne 1989 (Exh. "A");

(2) P449,793.43 covering customs duties paid for the month of October 1989 (Exh. "A-1").

They constitute statement of fact number 4 (Annexes A & A-1) in the Petition for Review and were admitted by Respondent in his answer. The total amount involved is only P616,782.49.

In view of all the foregoing, this Court hereby orders the refund of the amount of P616,782.49 to Petitioner.

SO ORDERED.

Quezon City, Metro Manila, May 31, 1993.

RAMON O. DE VEYRA
Associate Judge

WE CONCUR:

Abstain - I appeared as counsel of Petitioner in this case in the Bureau of Customs. Ernesto D. Acosta

ERNESTO D. ACOSTA
Presiding Judge

MANUEL K. GRUBA
Associate Judge

C E R T I F I C A T I O N

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