REPUBLIC OF THE PHILIPPINES
Court of Tax Appeals
QUEZON CITY

SECOND DIVISION

KELPHIL, INC.,
Petitioner,

C.T.A. CASE NO. 7064

Members:

\- versus -

CASTAÑEDA, JR., *Chairperson*
UY, *and*
PALANCA-ENRIQUEZ, *JJ.*

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:

JAN 0 8 2007

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DECISION

UY, *J*.:

This case involves a claim for refund in the amount of Three Million Six Hundred Forty Four Thousand Five Hundred Forty Nine Pesos and 67/100 (P3,644,549.67) allegedly representing excess or unutilized input value-added tax (VAT) on domestic sales of goods and services attributable to its zero-rated sales for the third quarter of 2002 up to the fourth quarter of 2003 .

THE FACTS

Petitioner is a corporation duly organized and existing under and by virtue of the laws of the Republic of the Philippines with principal office and place of business at the 28th Floor, Antel Global Corporate Center, 3 Doña Julia Vargas Avenue, Ortigas Center, Pasig City. It is engaged in the business of providing and exporting architectural and structural design services to non-resident foreign clients.[1] Petitioner is registered as a VAT entity evidenced by Certificate of Registration No. OCN 3RC0000174570.[2]

Respondent, on the other hand, is the duly authorized government official to grant refunds or tax credits of erroneously or illegally collected taxes, among others, with office address at the BIR National Office Building, Diliman, Quezon City.

On various dates, petitioner entered into service agreements with a Japanese company, Kawatetsu Engineering Ltd. of Japan (subsequently changed to JFE SEKKEI LTD.) for the supply to the latter of certain engineering, drawing and design works for the Kawatetsu's various projects in Japan.[3] These services were allegedly paid for in US dollars inwardly remitted by way of telegraphic transfers to petitioner's dollar accounts in its Philippine depositary banks. Petitioner claims that the said sales of services are zero-rated for VAT purposes pursuant to Section 4.102-2(b) of Revenue Regulations (R.R.) No. 7-95, as amended by Section 3 of Revenue Regulations (R.R.) No. 6-97.

For the third quarter of 2002 up to the fourth quarter of 2003,[4] petitioner allegedly incurred net input VAT on its domestic purchases of goods and services which were all attributable to its zero-rated sales, to wit:

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[1] Exhibits "A and A-1".
[2] Exhibit "B".
[3] Exhibits "R, S and T".
[4] July 1, 2002 up to December 31, 2003.

QUARTER	EXHIBIT	DATE FILED	ZERO-RATED SALES	INPUT VAT
3rd, 2002	C	10/25/02	11,715,255.09	96,849.96
4th, 2002	D	1/27/03	5,628,610.05	249,216.11
1st, 2003	E	4/25/03	7,015,868.89	321,707.57
2nd, 2003	F	7/25/03	8,539,972.05	232,385.37
3rd, 2003	G	10/27/03	14,950,089.26	358,464.85
4th, 2003	H	1/26/04	________	176,666.71
Total			**47,849,795.34**	**1,435,290.57**

On September 27, 2004, petitioner simultaneously filed with the Bureau of Internal Revenue (BIR) its amended quarterly VAT returns for the third quarter of 2002 up to fourth quarter of 2003 reflecting an increased unutilized input VAT of P3,644,549.67, computed as follows:

Exh	Quarter Involved	Zero-Rated Sales	Taxable Sales	Output VAT (a)	INPUT VAT This Quarter (b)	INPUT VAT Excess [(c) =(a)-(b)]
	2002					
I	3rd qtr	P11,511,381.02	P -	P -	P 597,524.03	P 597,524.03
J	4th qtr	10,200,033.49	-	-	454,568.69	454,568.69
	2003					
K	1st qtr	11,545,248.25	-	-	647,289.98	647,289.98
L	2nd qtr	14,414,890.54	-	-	683,059.38	683,059.38
M	3rd qtr	13,846,446.90	-	-	618,236.47	618,236.47
N	4th qtr	14,097,259.89	562,923.00	54,230.00	698,101.12	643,871.12
	TOTAL	**P75,615,260.09**	**P562,923.00**	P54,230.00	**P3,698,779.67**	**P3,644,549.67**

On the next day, September 28, 2004, petitioner filed with the BIR two (2) letters together with the Applications for Tax Credits/Refunds (BIR Form No. 1914), requesting for the refund/tax credit of input tax payments for the third and fourth quarters of 2002 and all the four quarters of 2003 in the respective amounts of P1,052,092.72 and P2,592,456.95 or in the sum P3,644,549.67.[5]

On September 30, 2004, petitioner filed the instant Petition for Review.

For failure of the respondent to file his Answer within the period given by this Court, he was declared in default. Consequently, petitioner was allowed to present testimonial and documentary evidence *ex-parte* and this case was considered submitted for decision on June 27, 2006 after the petitioner has filed its memorandum. Hence, this decision.

THE ISSUE

The lone issue to be resolved in this case is whether or not petitioner is entitled to the refund of the amount of P3,644,549.67 allegedly representing excess or unutilized input VAT on its domestic purchases of goods and services attributable to zero-rated sales for the period covering the third quarter of 2002 up to the fourth quarter of 2003.

THE COURT'S RULING

Upon careful scrutiny of the evidence adduced solely by petitioner, this Court finds legal basis to grant the petition, but not for the entire amount claimed as will be explained later.

Petitioner anchors its claim for refund of excess input VAT payments under Section 112(A) of the National Internal Revenue Code (NIRC) of 1997, as amended, which provides:

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5 Exhibits "O, O-2, P and P-2".

> "*SEC. 112. Refunds or Tax Credits of Input Tax. –*
>
> (A) Zero-rated or Effectively Zero-rates 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 a case of zero-rated sales under Section 106 (A)(2)(a)(1), (2) and (B) and Section (B)(1) and (2), the acceptable foreign currency proceeds thereof have 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 or effectively zero-rated sale and also in taxable or exempt sale of goods or properties or services, and the amount of creditable input tax due or paid cannot be directly or entirely attributed to any one of the transactions, it shall be allocated proportionately on the basis of the volume of sales."

From the foregoing, in order to be entitled to a refund of unutilized input VAT payments attributable to zero-rated sales or effectively zero-rated sales, the following requisites must be complied with:

1) there must be zero-rated or effectively zero-rated sales;
2) that input taxes were incurred or paid;
3) that such input VAT payments are directly attributable to zero-rated sales or effectively zero-rated sales;
4) that the input VAT payments were not applied against any output VAT liability; and
5) that the claim for refund was filed within the two year prescriptive period.[6]

Anent the first requisite, petitioner asserts that it rendered engineering, drawing, design services to its non-resident foreign client, JFE SEKKEI LTD. The services performed by petitioner to JFE SEKKEI LTD. are classified as zero-rated under Section 4.102-2(b)(2) of R.R. No. 7-95, as amended by R.R. No. 6-97, which provides:

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[6] American Express International, Inc.- Philippine Branch vs. CIR, CTA E.B. No. 103, March 3, 2006.

> "*SEC. 4.102-2. Zero-Rating.* – xxx
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> (b) Transactions Subject to Zero-Percent (0%) Rate. - The following services performed in the Philippines by VAT-registered persons shall be subject to zero-percent (0%) rate:
>
> (1) x x x;
>
> (2) Services other than processing, manufacturing or repacking for other persons doing business outside the Philippines of goods which are subsequently exported, as well as services by a resident to a non-resident foreign client, such as project studies, information services, engineering and other architectural designs and other similar services, the consideration for which is paid in acceptable foreign currency and accounted for in accordance with the rules and regulations of BSP."

Petitioner presented numerous documents such as service agreements, summary of zero-rated service income and collection, billing letters, official receipts and credit advices[7] to prove that for the subject period, it actually generated revenues in the amount of P75,615,260.09 for rendering certain engineering and design work services to JFE SEKKEI LTD. The foreign proceeds from the said sales of services in the amount of US$1,403,494.41[8] were inwardly remitted and accounted for in accordance with the rules and regulations of the Bangko Sentral ng Pilipinas (BSP).

We find petitioner's argument tenable. Clearly, petitioner's sales of services for the last two (2) quarters of 2002 and four (4) quarters of 2003 amounting to P75,615,260.09 qualify as zero-rated sales under Section 108(B)(2) of the NIRC of 1997, as amended, which reads:

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[7] Exhibits "R, S, T, V-1 to V-50, W-1 to W-58, X-1 to X-67, Y-1 to Y-83, Z-1 to Z-76 and AA-1 to AA-65".
[8] See page 2 of CPA report (Exhibit "U")..

> "*SEC. 108. Value-Added Tax on Sale of Services and Use or Lease of Properties.* –
>
> (A) xxx
>
> (B) Transactions Subject to Zero Percent (0%) Rate. — The following services performed in the Philippines by VAT-registered persons shall be subject to zero percent (0%) rate:
>
> (1) Processing, manufacturing or repacking goods for other persons doing business outside the Philippines which goods are subsequently exported, where the services are paid for in acceptable foreign currency and accounted for in accordance with the rules and regulations of the Bangko Sentral ng Pilipinas (BSP);
>
> (2) Services other than those mentioned in the preceding paragraph, the consideration for which is paid for in acceptable foreign currency and accounted for in accordance with the rules and regulations of the Bangko Sentral ng Pilipinas (BSP)."

Concerning the second requisite, the commissioned independent CPA, Mr. Roque S. Fado, noted in his report dated October 21, 2005,[9] that out of the total reported input VAT of P3,698,779.67, the amount of P153,734.50 detailed below was not duly substantiated:

1. Input taxes claimed on purchases of goods/services supported by documents not in the name of the Company (these are presented in Schedule 3 totaling Php3,770.27);

2. Input taxes claimed erroneously computed (as shown in Schedule 4, the amount of input taxes claimed was overstated by Php112,756.03); and

3. Input taxes claimed on purchases of goods/services not supported by documents (input taxes claimed not supported by documents totaled Php37,208.20 as shown in Schedule 5).

Furthermore, upon careful scrutiny of the said report, the input taxes of P35,315.27 should likewise be disallowed due to the following reasons:

[9] Exhibit "U".

Supplier	Exhibit	Date	Invoice Amount	Input VAT
a. Input VAT claimed on purchase of service supported by official receipt not in the name of the company				
KRA Corporation	GG-187	7/31/2003	P 12,476.00	P 1,134.18
b. Input VAT claimed on purchase of service supported by NON-VAT or TAN official receipt				
LTC Printing Press	DD-128	1/8/2003	P 17,250.00	P 1,568.18
JapanPNB Leasing & Finance Corp.	FF-133	5/6/2003	32,205.75	1,298.75
Designed Power, Inc.	EE-54	2/17/2003	319,982.40	29,089.32
Subtotal			P369,438.15	P31,956.25
c. Input VAT claimed on purchase of service not supported by official receipt				
Upstart Ventures	CC-55	7/16/2002	P 176.00	P 16.00
Upstart Ventures	CC-56	7/18/2002	33.00	3.00
Upstart Ventures	CC-61	7/19/2002	120.00	10.91
Upstart Ventures	CC-62	7/19/2002	120.00	10.91
Agram Trading, Inc	EE-131	3/2/2003	193.60	17.60
Subtotal			P 642.60	P 58.42
d. Input VAT claimed on purchase of service supported only by Statement of Account, Statement Summary				
Smart Communications	EE-70	2/21/2003	P 2,057.50	P 187.05
Smart Communications	EE-71	2/21/2003	2,102.04	191.09
Smart Communications	DD-71	11/25/2002	5,172.17	470.20
Smart Communications	DD-122	12/31/2002	2,407.98	218.90
Smart Communications	DD-123	12/16/2002	3,819.60	347.23
Smart Communications	DD-140	1/16/2003	6,119.22	556.29
Smart Communications	DD-141	1/16/2003	2,152.28	195.66
Subtotal			P 23,830.79	P 2,166.42
Total			P406,387.54	P35,315.27

Therefore, petitioner was only able to substantiate by valid VAT invoices or receipts the input VAT of P3,509,729.90, computed hereunder:

Reported Input VAT		P 3,698,779.67
Less:	Disallowances	
	Per CPA Report	P 153,734.50
	Per this Court's further verification	35,315.27
	Total Disallowances	P 189,049.77
Substantiated Claim		P 3,509,729.90

With regard to the third requisite, the amended VAT returns for the third quarter of 2002 until the fourth quarter of 2003 disclose that not all of the substantiated input VAT of P3,509,729.90 is attributable to zero-rated sales. In its amended VAT return for the fourth quarter of 2003, petitioner had taxable sales in the amount of P562,923.00 with the corresponding output VAT of P54,230.00. Hence, only the net input VAT of P3,455,499.90 (P3,509,729.90 less P54,230.00) directly pertains to petitioner's zero-rated sales of P75,615,260.09.

As to the fourth requisite, petitioner deducted the claimed excess input VAT for each quarter as "Any VAT Refund/TCC Claimed" in the corresponding amended quarterly VAT returns for the period July 1, 2002 up to December 31, 2003.[10] Thus, petitioner proved that no amount of the claimed excess input VAT was carried-over or applied against any output tax in the succeeding taxable quarters.

Finally, petitioner likewise complied with the fifth requisite. It timely filed both the administrative and judicial actions for refund/tax credit on September 28, 2004 and September 30, 2004, respectively, within the two (2)-year reglementary period pursuant to the provisions of the NIRC of 1997, as amended, reckoned from October 25, 2002, the date of filing of the earliest quarter covered by the instant claim.

WHEREFORE, premises considered, the Petition for Review is hereby **PARTIALLY GRANTED**. Accordingly, respondent is **ORDERED TO REFUND** to petitioner the reduced amount of Three Million Four Hundred Fifty Five Thousand Four Hundred Ninety Nine Pesos and 90/100 (P3,455,499.90) representing excess or unutilized input VAT attributable to zero-rated sales for the third

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[10] Exhibits "I-5, J-5, K-5, L-5, M-5 and N-5".

quarter of 2002 up to the fourth quarter of 2003.

SO ORDERED.

ERLINDA P. UY
Associate Justice

WE CONCUR:

JUANITO C. CASTAÑEDA, JR.
Associate Justice

OLGA PALANCA-ENRIQUEZ
Associate Justice

ATTESTATION

I attest that the conclusions in the above Decision were reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

JUANITO C. CASTAÑEDA, JR.
Associate Justice
Chairperson

CERTIFICATION

Pursuant to Article VIII, Section 13 of the Constitution, and the Division Chairperson's Attestation, it is hereby certified that the conclusions in the above Decision were reached in consultation before the case was assigned to the writer of the opinion of the Court.

ERNESTO D. ACOSTA
Presiding Justice