REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

FIRST DIVISION
****

SAN ROQUE POWER CORPORATION,
Petitioner,

- versus -

C.T.A. CASE NO. 6213

Members:

ACOSTA, *Chairman*
BAUTISTA, and
CASANOVA, *JJ.*

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:
DEC 2 3 2004

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DECISION

ACOSTA, E., PJ.:

Before Us is a petition for review seeking a refund and/or issuance of a tax credit certificate in the amount of Three Hundred Fourteen Million Five Hundred Eight Thousand Six Hundred Eighty Five Pesos and 49/100 (P314,508,685.49) allegedly representing unutilized input Value Added Tax ("VAT") on purchases of capital goods and other taxable goods and services for the period covering December 1998 to September 1999.

San Roque Power Corporation (hereinafter referred to as "petitioner"), a corporation duly organized and existing under and by virtue of the laws of the Republic of the Philippines, is engaged in the business of generating and supplying electricity. It is registered with the Bureau of Internal Revenue with certificate of registration bearing RDO Control No. 98-006-007934 dated August 31, 1998.[1]

On October 11, 1997, petitioner and the National Power Corporation (hereinafter referred to as "NPC") entered into a Power Purchase Agreement ("PPA") for the design, construction, installation, completion, testing, commission, and operation of the San Roque Multipurpose Project for twenty five-(25) years on a Built Operation Transfer ("BOT") scheme of the government. The parties agreed that during the twenty five (25) year period, petitioner shall distribute electricity which shall be sold and purchased to NPC.[2] Under the said program, petitioner is obligated to turnover the hydro electric plant located at San Manuel Pangasinan to the government after twenty five (25) years.[3]

From December 1998 to September 1999, petitioner purchased capital goods and availed services relative to the construction of the San Roque Multipurpose Project, pursuant to the PPA Contract with the NPC.

On February 12, 1999, respondent and the Department of Finance issued VAT Review Ruling No. 015-99 which provides that transactions involving the purchase of

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[1] Rollo, pp. 1-2 & Annex B to the petition for review
[2] Rollo, p. 2
[3] TSN dated May, 2, 2001, p.13

electricity from independent power producers shall be subject to VAT at zero rate percent.[4] Under the said ruling, petitioner secured approval on its VAT applications from respondent for the third and fourth taxable quarters of 1998; taxable year 1999; taxable year 2000; fourth taxable quarter of 2001 and taxable years 2002 and 2003.[5]

Petitioner seasonably filed its quarterly VAT returns for the period December 1, 1998 to September 30, 1999.[6]

On August 10, 1999 and November 25, 1999, petitioner amended its quarterly VAT returns for the quarters ending March 31, 1999 and September 30, 1999.[7] The total input VAT incurred on the project was solely borne by petitioner.[8] The amended returns reflected excess input VAT payments in the amount of Three Hundred Fourteen Million Five Hundred Eight Thousand Six Hundred Eighty Five Pesos and 49/100 (P314,508,685.49) arising from its purchases of capital goods and other taxable goods and services[9], broken down as follows:

PERIOD	EXHIBIT	DATE FILED	OUTPUT VAT	Input Tax Carried Over from previous quarter	INPUT VAT on Domestic Purchases	Total Available Input Tax
4th Quarter of 1998	A	January 25, 1999	-		P24,954,362.50	P 24,954,362.50
Amended 1st Qtrly. VAT return for 1999	C	August 10, 1999	-	P 24,954,362.50	94,747,576.01	119,701,938.50
1st Quarter of 1999	B	April 12, 1999	-	24,954,362.50	94,741,388.48	119,695,751.00
2nd Quarter of 1999	D	August 10, 1999	-	119,701,938.50	62,006,101.46	181,708,040.00

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4 Exhibit J
5 Exhibits N, O, KK, LL & MM; TSN dated June 5, 2001, p. 15
6 Rollo, p. 65, Joint Stipulation of Facts and Issues
7 Rollo, p. 3
8 Rollo, p. 158
9 Rollo, p.65, Joint Stipulation of Facts and Issues

3rd Quarter of 1999	E	October 25, 1999	-	181,708,040.00	110,313,145.17	292,021,185.17
Amended 3rd Qtrly. VAT return for 1999	F	Nov. 25, 1999	-	181,708,040.00	132,800,645.49	314,508,685.49

On December 22, 1999, petitioner filed a claim for refund of its unutilized VAT payments with the respondent. [10]

On December 28, 2000, the petitioner instituted a petition for review before this Court to toll the running of the two-year prescriptive period on account of respondent's inaction on its claim for refund.[11]

In answer to the petition, respondent interposed the following special and affirmative defenses:

> *1. Petitioner's claim for input tax refund/credit is still undergoing administrative routinary evaluations, investigation/examination by the respondent-Bureau;*
> *2. Petitioner failed to show that it has complied with the provisions of Revenue Regulations 7-95 or the consolidated Value Added Tax Regulations particularly Sec. 9.296.1(d) on compliance requirements;*
> *3. Petitioner miserably failed in its allegations that capital goods purchased were actually used in the construction of the San Roque Multi-Purpose project;*
> *4. The total amount of P314,508,685.49 being claimed by petitioner as alleged unutilized input tax credits for the period December 1998 to September 1999 was not substantiated by documents pursuant to Section 4.110.5 of Revenue Regulations No. 7-95 (Consolidated Value Added Tax Regulations);*
> *5. In an action for tax refund/credit, the burden of proof is on the taxpayer to establish its right to refund and failure to sustain the burden is fatal to such claim for refund/credit and*
> *6. Claims for refund/credit are in the nature of tax exemption, hence, construed strictissimi juris against the taxpayer.*[12]

[10] Exhibit G
[11] Rollo, p. 1; par. 9, Joint Stipulation of Facts and Issues
[12] Rollo, p. 32

Petitioner availed the services of an independent certified public accountant (CPA) due to the voluminous nature of the evidence to be presented. Acting on petitioner's motion, this Court issued an order dated June 6, 2001, authorizing Ms. Feliza A. Peralta of the Sycip Gorres Velayo firm as an independent certified public accountant to audit, examine, verify voluminous documents consisting of receipts, invoices, vouchers and similar documents.[13] Pertinent excerpts on the findings of the commissioned CPA disclosed the following:

> *Based on our review and validation, the amount of said claim that we ascertained to be substantiated by supporting documents is P276,837,501.16, computed as follows:*

Quarter	Year	Ref. No.	On Construction Work in Progress	On Pre-operating Expenses	Total
4th	1998	*Exhibit R3 Annex 2*	P24,878,657.21	-	P24,878,657.21
1st	1999	*Exhibit R4 Annex 3*	92,316,745.91	P45,023.76	92,361,769.67
2nd	1999	*Exhibit R5-2 Annex 4-2*	61,273,390.84	10,175.75	61,283,566.59
3rd	1999	*Exhibit R6-5 Annex 5-5*	98,231,388.58	82119.14	98,313,507.72
TOTAL			P276,700,182.54	P137,318.65	**P276,837,501.19**
Less: Discrepancy between the amended VAT return for the 1st quarter of 1999 and Summary List of Purchases (and amount claimed for refund) as presented in item 12 below					0.03
TOTAL INPUT VAT PROPERLY SUBSTANTIATED					**P276,837,501.16**

[13] Rollo, p. 77

> *The Company's claim which we were not able to validate amounted to P37,671184.33 x x x.*[14]

After each party proffered their testimonial and documentary evidence and filed their respective memoranda, the case was submitted for resolution.

The parties jointly stipulated the following issues for the consideration of the Court:

1. *Whether or not petitioner has incurred excess input taxes in the amount of P314,508,685.49 for the period December 1, 1998 to September 30, 1999 on its purchases of capital goods and other taxable goods and services and whether the same are properly substantiated by VAT invoices and receipts;*

2. *Whether or not the amount of input VAT sought to be refunded by the petitioner was actually incurred or arose from the purchase of capital goods for the construction of the San Roque Power Multipurpose Project, pursuant to Section 112(B) of the NIRC, as amended, in relation to Section 4.106-1 (b) of Revenue Regulations No. 7-95, as amended, and/or other rules and regulations governing the refund of excess input VAT;*

3. *Whether or not the amount of input VAT incurred by the petitioner in the purchase of other taxable goods and services utilized in the construction of the San Roque Power Multipurpose Project is refundable, pursuant to Section 112 (A) of the NIRC, as amended, in relation to Section 4.106-1(a) of Revenue Regulations No. 7-95, as amended, and other rules and regulations governing this refund of excess input VAT;*
4. *Whether or not Petitioner has applied or utilized its accumulated input VAT incurred on the purchases of capital goods and services for the period of December 1, 1998 to September 30, 1999 to the succeeding taxable quarters;*

5. *Whether or not petitioner is entitled to a tax credit certificate/refund in the amount of P314,508,685.49 representing unutilized input VAT allegedly paid on its purchases of capital goods and other taxable*

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[14] Exhibits R1-2 to R1-4 of the Report on the Results of the Procedures Performed for the Claim for Refund/TCC of Unutilized Input VAT for the period December 1998 to September 1999

> *goods and services for the period December 1, 1998 to September 30, 1999.*[15]

The first, second, third and fifth issues shall be jointly discussed as they are interrelated. The crux of the controversy is whether or not petitioner is entitled to a refund in the amount of P314,508,685.49 on its unutilized input VAT payments .

Petitioner cites as legal bases of its claim of refund, the provisions of Sections 112 (A) and (B) of the 1997 Tax Code which read:

> *Section 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 where 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 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 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.*

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[15] Rollo, p. 388

The provision of Section 112 (A) of the 1997 Tax Code mandates that in order to claim for a refund/tax credit of input VAT, there must be zero-rated sales or effectively zero-rated sales to which the input VAT sought to be refunded are attributable.[16] A cursory examination of the quarterly VAT returns submitted *(Exhibits A, B, C, D & E)* reveals that petitioner had no record of zero-rated sales or effectively zero-rated sales. Thus, Section 112(A) afore-cited can not apply in the instant case. Petitioner, therefore, can only claim for a refund/tax credit of its input VAT on capital goods based on Section 112(B). Under the said provision, there is no requirement that the input taxes sought to be refunded be attributable to zero-rated sales or effectively zero-rated sales.

Supplementary to the provision of Section 112(B) of the 1997 Tax Code is Section 4.106-1(b) of Revenue Regulations No. 7-95 which provides:

> *Section 4.106-1. Refunds or tax credits of input tax. – xxx*
>
> *x x x xxx 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.*

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[16] Epson Precision (Philippines) Inc. vs. Commissioner of Internal Revenue, C.T.A. Case No. 6184, November 17, 2003, and Placer Dome Technical Services (Philippines), Inc. vs. Commissioner of Internal Revenue, C.T.A. CASE NO. 6106, May 14, 2002

Plainly from the aforementioned provisions of Section 112(B) of the 1997 Tax Code and Section 4.106-1(b) of Revenue Regulations 7-95, before petitioner can claim for a refund, it must prove compliance with the following requirements:

1) *That it is a VAT registered entity;*
2) *That input taxes claimed were paid on capital goods duly supported by VAT invoices and official receipts;*
3) *That it did not offset or apply the claimed input VAT payments on capital goods against any output VAT liability; and*
4) *That the claim for refund was filed within the two year prescriptive period both in the administrative and judicial levels (**Telecommunications Technologies Philippines, Inc vs. CIR, CTA Case No. 6018, November 24, 2003**).*

Petitioner as a VAT registered entity is not disputed as manifested in the parties' joint stipulation of facts.[17]

As to the second requirement, petitioner argues that it purchased capital goods and rendered services related thereto, duly substantiated by official receipts and invoices which warranted refund of excess input VAT.

Section 4.106-1(b) of Revenue Regulations No. 7-95 defines capital goods as 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.[18]

Petitioner's acquisition of materials and services rendered for the construction of the power station, dam and spillway are classified as capital goods as reiterated in the case of

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[17] Rollo, p. 65
[18] Rio Tuba Nickel Mining Corporation vs. CIR, Feb. 3, 2004, CTA Case No. 6293

Hopewell Power (Philippines) Corp vs. Commissioner of Internal Revenue,[19] wherein We 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.***

In the case of ***Rohm Apollo Semiconductor Philippines Inc. vs. Honorable Commissioner of Internal Revenue***[20], this Court included cost of services within the purview of the term "capital goods", to wit:

> *The cost of services is within the scope and meaning of the term "capital goods" if the same form part of the cost of a capital asset.*

We agree with the findings of the commissioned CPA in outrightly denying the amount of P37,671,184.33 for not being substantiated by official receipts and invoices.[21] The commissioned CPA considered the amount of P276,837,501.16 as duly validated.

After a careful scrutiny of the records, We rule that only the aggregate amount of P274,702,025.63, duly supported by official invoices and/or receipts should be classified as capital goods, detailed as follows:

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[19] CTA Case No. 5389, January 4, 1999 (See Wrigley Philippines Inc. vs. CIR, July 12, 2002, CTA Case No. 5939)
[20] CTA Case No. 6534, May 27, 2004
[21] Exhibits R1-2 to R1-4 of the Report on the Results of the Procedures Performed for the Claim for Refund/TCC of Unutilized Input VAT for the period December 1998 to September 1999

EXHIBIT	NAME of SUPPLIER	PARTICULAR	REFERENCE OR/Invoice	INPUT VAT
P1-1 to P1-2	Sithe Philippines Holdings, Inc	Development & Mgt Fee	OR # 001 & 003	24,878,657.21
P2-1	Sithe Philippines Holdings, Inc	Construction Mgt Fee	OR # 004	740,434.09
P2-12 to P2-15	Raytheon Ebasco Overseas Ltd.	Construction Progress Billing	OR # 0004 to 0007	91,169,665.69
P2-25	Asia Soft	Computer set & server	Inv # 074	34,863.64
P3-6 to P3-9	Raytheon Ebasco Overseas Ltd.	Construction Progress Billing	OR # 0008 to 11	60,400,502.11
P3-10	Sithe Philippines Holdings, Inc	Construction Mgt Fee	OR # 006	690,032.73
P4-7 to P4-10	Asia Soft	Network Hardware, AVR, LAN card	OR# 038, 041, 099 &100	11,249.94
P4-17	Comcore Technologist Corp	Expansion card	Inv#0299	1,589.55
P4-48	McGala Pacific (Philippines), Inc.	1 unit Philips Genie & reg.	OR#8133	1,622.27
P4-95 to P4-99	Raytheon Ebasco Overseas Ltd.	Construction Progress Billing	OR # 0012 to 0016	74,266,245.52
P4-109 to P4-110	Telecommunication Distributors	Cellphone units	Inv # 753591 & 753595	19,662.55
P4-114	Raytheon Ebasco Overseas Ltd.	Construction Progress Billing	OR # 0017	22,487,500.33
T O T A L				274,702,025.63

This Court denies petitioner's claim for refund on the input VAT paid on "pre-operating expenses" and "construction work" in the amounts of P137,318.65 and P1,998,156.91, respectively.

Pre-operating expenses should be excluded as these purchases are not necessary in the construction of the power plant facilities and the nature of some of these purchases are not capable of determination.

As for the disallowed amounts of input taxes on "construction work in progress", the detailed explanation are shown below.

ITEM	REFERENCE	SUPPLIER	INPUT VAT
A) Input VAT supported by Quarterly VAT returns filed by petitioner in behalf of its suppliers			
	P2-3 to 5	Sigma Consultants	P 39,329.16
	P2-6 to 8	Malcolm Pirnie	234,676.12
	P2-9 to 11	Cunningham Resources	36,364.84
	P3-13 to 15	Agra Earth & Environmental	182,856.00

P4-19 to24	Cunningham Resources	329,498.27
P4-35 to 37	Harza Engineering Company Int'l	670,581.32
P4-88 to93	R.W. Beck	146,579.93
B) Input VAT the nature of purchases are not capable of determination		
P2-26	Mandarin Oriental	58,953.28
P4-106	Strategic Edge Inc.	19,090.91
P4-43	La Milagrosa	2,100.00
P4-44	Louis Berger International Phil Inc	31,495.48
C) Input VAT which are not capitalizable		
P2-30	Garden Marketing	2,459.09
P4-11	Asia Soft	545.45
D) Input VAT the nature of services is not capable of determination whether or not it forms part of construction		
P4-4 to 6a	Asian Insights Inc.	70,284.74
T O T A L		**P1,998,156.91**

Anent the third requirement, petitioner did not offset its input VAT claimed against any output VAT liability as it had not commenced operations from December 1998 to September 1999. Logically, petitioner could not have generated any output tax liability to which the input VAT may be applied or credited.[22]

With regard to the fourth requirement on prescription, the earliest quarter covered by the subject claim was the last taxable quarter of 1998 when petitioner filed its VAT return on January 25, 1999. Counting from this date, the claim for refund filed on December 22, 1999 in the administrative level[23] and petition for review filed on December 28, 2000 fall within the two year prescriptive period.[24] Claims for refund, both in the administrative and

[22] Exhibits A, B, C, D, E & F
[23] Rollo, p. 59
[24] Rollo, p. 1

judicial levels should be filed within the two year period from the date of filing of the original quarterly VAT return.[25]

Finally, as to the issue on whether or not petitioner applied or utilized its accumulated input VAT to the succeeding quarters, We rule in the negative.

The VAT return for the fourth quarter of 1999 indicated that the input tax of P314,508,685.49 (covering the 4th quarter of 1998 to the four quarters of 1999) was deducted as "any VAT refund or TCC claimed" from the total available input taxes of P367,409,236.16 as of the fourth quarter of 1999. Thus, the resulting excess input taxes of P52,900,550.67 to be carried over to the succeeding quarters of taxable year 2000 no longer included the claimed input taxes of P314,508,685.49.[26] The rationale for the deduction is to ensure that petitioner can no longer avail of another refund on the same amount claimed, to the detriment of the government.[27]

IN VIEW OF THE FOREGOING, the petition for review is hereby **GRANTED**. Accordingly, respondent is hereby **ORDERED** to **REFUND** or in the alternative, to **ISSUE A TAX CREDIT CERTIFICATE** in favor of petitioner in the reduced amount of P274,702,025.63 representing unutilized input VAT for the period December 1998 to September 1999.

SO ORDERED.

ERNESTO D. ACOSTA
Presiding Justice

[25] Magellan Cogeneration Inc. vs. CIR, May 19, 2003, CTA Case No. 6033 and Telecommunications Technologies Philippines, Inc. versus CIR, C.T.A. Case No. 6018, Nov. 24, 2003
[26] Rollo, p. 226
[27] BASF Philippines Inc. vs. CIR, CTA Case No. 6715, March 20, 2002

WE CONCUR:

LOVELL R. BAUTISTA
Associate Justice

CAESAR A. CASANOVA
Associate Justice

CERTIFICATION

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

ERNESTO D. ACOSTA
Chairman, First Division
Presiding Justice