REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

SPECIAL THIRD DIVISION

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DEUTSCHE KNOWLEDGE SERVICES, PTE. LTD.,
Petitioner,

- versus -

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

CTA CASE NO. 9154

Members:

UY, *Chairperson*,
RINGPIS-LIBAN, *and*
MODESTO-SAN PEDRO, *JJ.*

Promulgated:

MAY 2 3 2023
C — 1:12 p.m.

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RESOLUTION

UY, J.:

For resolution is respondent's ***Motion for Partial Reconsideration (Re: Amended Decision promulgated 24 March 2023)*** filed on May 2, 2023, with petitioner's ***Comment (Re: Motion for Reconsideration dated April 28, 2023)*** filed on May 16, 2023.

In his *Motion for Partial Reconsideration*, respondent seeks that the Amended Decision promulgated on March 24, 2023 be reversed and set aside. The dispositive portions of the assailed Amended Decision reads:

Amended Decision dated March 24, 2023

> "**WHEREFORE**, in consideration of the foregoing findings and discussions, the instant *Petition for Review* is **PARTIALLY GRANTED**. Accordingly, the dispositive portion of the Court's Decision dated October 4, 2019 is hereby **MODIFIED** to read as follows:

"**WHEREFORE**, in light of the foregoing consideration, the Petition for Review is **PARTIALLY GRANTED**. Accordingly, respondent is **ORDERED TO REFUND OR ISSUE A TAX CREDIT CERTIFICATE** in favor of petitioner in the amount of **₱14,619,389.11**, representing petitioner's excess and unutilized input VAT attributable to its zero-rated sales for the 3rd quarter of CY 2013.

SO ORDERED."

Respondent's arguments:

Respondent stresses that a tax refund is in the nature of a tax exemption which must be construed *strictissimi juris* against the taxpayer. The taxpayer must present convincing evidence to substantiate a claim for refund.

Allegedly, the law requires only "creditable input taxes" that are "directly attributable" may be refunded. In this case, no attributability was established between the input tax on purchases vis-à-vis petitioner's zero-rated sales. Since this is a claim for refund, petitioner must establish its claim by the quantum of evidence and not by assumption.

Respondent reasons that it is part of mandatory judicial notice that the Value Added Tax (VAT) system was adopted from Europe, and introduced in the Philippines in 1988 via Executive Order No. 273.[1] The VAT system was not a mere creation but rather a European system adopted by the Philippines. As it works in Europe, only the VAT paid for supplies in the business is creditable as an input tax of a VAT registered person. Thus, purchases must in turn relate to the supplies (goods/services) of a person makes. Not all input tax accumulated by a person may be claimed.

As it is in Europe, not all input tax from purchases by a business is creditable as input tax, but rather only those "related" to the supplies made can be claimed. Purchases by businesses such as personal activities, business entertainment, corporate events, and outside office meetings, cannot be claimed as an attributable and creditable input tax.

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[1] Adopting a Value-Added Tax, Amending for this Purpose Certain Provision of the National Internal Revenue Code, and for Other Purposes, effective January 1, 1988.

According to the respondent, this is the same in Philippine laws; that Section 112(A) of the National Internal Revenue Code (NIRC) of 1997, as amended, does not state that all input taxes of a VAT-registered person whose sales are zero-rated are refundable. Rather, Section 110(A) of the NIRC of 1997, as amended, determines what "creditable input taxes" are, and these are input taxes on purchases of goods which must be a factor in the chain of production in order to be creditable, consistent with the universal definition of VAT as essentially a "tax on transactions". The same is imposed at every stage of the distribution process on the sale, barter, exchange of goods or property and in the performance of services until it finally reaches the consumer. Hence, to be creditable, the input tax must either come from purchases of goods that form part of the finished product of the taxpayer, or be directly used in the chain of production.

Moreover, respondent contends that after determining which input taxes are "creditable", there is still a need to determine which creditable input taxes are attributable; that the connection between the purchases and the finished product must be "concrete" and not "imaginary" or "remote". The respondent submits that the assailed Amended Decision did not show the direct attributability of the purchases or input tax to the finished product whose sale is zero-rated.

Petitioner's comment on respondent's Motion for Reconsideration:

Petitioner argues that respondent's direct attributability theory does not have a support in law or in jurisprudence.

Petitioner submits that a reading of Section 110(B) of the NIRC of 1997, shows that the word "attributable" functions as an adjective and merely describes the relation between input tax and zero-rated sales. In context, the word "attributable" only requires that the excess input tax must be due or related to a zero-rated activity.

Furthermore, petitioner argues that respondent's reliance on his interpretation on Section 112 of the NIRC of 1997 is misplaced. The said provision is explicit how the amount of creditable input tax attributable to zero-rated sales of a taxpayer engaged in both zero-rated and taxable sales is determined. In relation with the provision of Section 4.112-1 of Revenue Regulations No. 16-2005, as amended, there is nothing in the foregoing rules which states that the input tax needs to be directly attributable or a factor in the chain of production to the zero-rated sale in order for it to be creditable or refundable.

Lastly, petitioner contends that its claimed input VAT credits for the 1st to 4th quarters for CY 2013 are duly substantiated by appropriate documentary evidence and are attributable to petitioner's zero-rated sales for the year. The same has been amply proven and verified by the Court as shown in the assailed Amended Decision.

THE COURT'S RULING

Respondent's Motion for Partial Reconsideration lacks merit.

We find respondent's contention that in order for input tax to be creditable, the same must come from purchases of goods that form part of the finished product, or it must be directly used in the chain of production is misplaced, and thus, devoid of merit.

Section 112(A) of the NIRC of 1997,[2] as amended does not require that the input VAT must be "directly attributable" to zero-rated sales in order for it to be creditable.

The said provision expressly states that it only requires that the creditable input VAT should be "attributable" to the zero-rated or effectively zero-rated sales.

A careful reading of Section 112(A) of the NIRC of 1997, as amended, shows that the phrase "directly and entirely attributable" refers to instances wherein the taxpayer is engaged in zero-rated or effectively zero-rated sales and in taxable or exempt sales, and the input taxes cannot be directly or entirely attributed to any of the sales. The law allows the allocation of creditable input taxes which cannot be directly or entirely attributable to zero-rated sales, in which case, the input taxes shall be allocated proportionately on the bases of the volume sales.

Relative thereto, Section 110 of the NIRC of 1997, as amended, is clear as it provides that any input tax on the following transaction

[2] SEC. 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 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: x x x *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.**" (Emphases Added)

evidenced by a VAT invoice or official receipt shall be creditable against output tax, to wit:

"Sec. 110. *Tax Credits.* –

(A) Creditable Input Tax. –

(1) Any input tax evidenced by a VAT invoice or official receipt issued in accordance with Section 113 hereof on the following transactions **shall** be creditable against the output tax:

(a) Purchase or importation of goods:

(i) For sale; or

(ii) For conversion into or intended to form part of a finished product for sale including packaging materials; or

(iii) For use as supplies in the course of business; or

(iv) For use as materials supplied in the sale of service; or

(v) For use in trade or business for which deduction or depreciation or amortization is allowed under this Code

(b) Purchase of services on which a value added tax has been actually paid.

xxx xxx xxx

The foregoing provision shows that an input VAT evidenced by VAT invoice or official receipt is creditable against the output VAT is not only confined on the purchase or importation of goods "*for conversion into or intended to form part of a finished product for sale including packaging materials*," but also those purchase/importation of goods for sale, for use of supplies in the course of business, and for use in trade or business for which deduction for depreciation or amortization is allowed under the NIRC.

Thus, the respondent's contention that "to be creditable, the input tax must come from purchases of goods that form part of the finished product of the taxpayer or it must be directly used in the chain of production" is not entirely consistent with the above-quoted Section 110. This is so because the said provision, as clearly worded, did not limit itself to purchases or importation of goods which are to be converted into or intended to form part of a finished product for sale, or to be used in the chain of production; but also includes, among others, purchases or importation of goods for use as supplies in the course of business, or for use in trade or business for which deduction for depreciation or amortization is allowed; as well as purchases of services for which VAT has been actually paid.

Accordingly, provided that the subject input tax is evidenced by a VAT invoice or official receipt issued in accordance with Section 113 of the NIRC of 1997, as amended, the same may be creditable against the output VAT.

Based on the foregoing disquisitions, it is clear that there is no basis for the respondent to say that the input taxes on purchases of goods is only limited to those purchases that only form part of the finished product of the taxpayer.

In view of the foregoing, We find no compelling reason to modify or reverse Our findings and conclusions reached in the assailed Amended Decision.

WHEREFORE, in view of the foregoing considerations, respondent's ***Motion for Partial Reconsideration (Re: Amended Decision promulgated 24 March 2023)*** is **DENIED** for lack of merit.

SO ORDERED.

ERLINDA P. UY
Associate Justice

MA. BELEN M. RINGPIS-LIBAN
Associate Justice

(On Official Business)
MARIA ROWENA MODESTO-SAN PEDRO
Associate Justice