REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

RODOLFO A. GAMBOA,
Petitioner,

- versus - C.T.A. CASE NO. 4960

HONORABLE JOSE U. ONG,
COMMISSIONER OF INTERNAL
REVENUE,
Respondent.

Promulgated:
MAR 01 1995

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# DECISION

The issue presented in this case, which involves a claim for refund of the sum of P789.39 representing value-added tax (VAT), is whether or not the sale of molasses is exempt from VAT under Section 103 (b) of the Internal Revenue Code as amended, the pertinent provisions of which state as follows:

> Sec. 103. Exempt Transactions. - The following shall be exempt from the value-added tax:
>
> xxx xxx xxx
>
> (b) Sale or importation in their original state of agricultural and marine food products; livestock and poultry or a kind generally used as, or yielding or producing food for human consumption; and breeding stock and genetic materials therefor.
>
> Products classified under this paragraph and paragraph (a) shall be considered in their original state even if they have undergone the simple processes of preparation or preservation for the market, such as freezing, drying,

> salting, smoking or stripping. Polished and/or husked rice, corn grits and raw cane sugar shall be considered in their original state for purposes of this paragraph.

There is no dispute on the facts leading to this controversy. The amount of P789.39 representing VAT, surcharge and interest, on his sale of molasses was paid by the petitioner, a bona fide sugar producer, on December 5, 1991 under Payment Order No. 010618635 (Exh. "A") and Confirmation Receipt No. B 23755593 (Exh. "B"). On February 28, 1992, he filed a written request or claim for refund of said tax with the respondent contending that molasses, like raw cane sugar, is an agricultural product in its original state and therefore exempt from VAT under said Section 102 (b) of the Tax Code (Exh. "C"). In a letter, dated December 29, 1992 (Exh. "D"), respondent Commissioner of Internal Revenue denied petitioner's claim for refund on the ground that molasses, unlike raw cane sugar, is not included in the exemption under Section 103 (b) of the Tax Code and its implementing Revenue Regulations No. 5-87, as well as in BIR VAT Ruling No. 058-90. More extensively, the position of respondent as contained in his letter of December 29, 1992, states as follows:

*Please be informed that the issue on the taxability of the sale of molasses has been squarely resolved in VAT Ruling No. 058-90 dated February 28, 1990 wherein it was held that -*

> *"Generally, milling which employs technology and machinery, is not considered as a simple process for the purpose of qualifying agricultural products as remaining in their original state. Thus, all milled products with the exception of rice, corn grits and raw cane sugar, are no longer in their original state; hence not exempt from the VAT* (Section 103 (b) of the Tax Code as implemented by Section 9 (b)(2) of Rev. Reg. 5-87). *Molasses, although a by-product of sugar milling, is not however considered as raw cane sugar; hence its sale is subject to 10% VAT pursuant to Section 100 of the same Code."*

*Likewise, the VAT Review Committee, in the same ruling, held that there is no inconsistency between the provisions of the VAT law and those of the implementing regulations. It stated that -*

> *"Section 100 of the same Code imposes a 10% VAT on the sale of goods except those specifically enumerated under Section 103 of the same Code. It is very clear under the law that molasses is not included among those qualified for exemption under subsection (b). In fact, Section 9 (b)(2) of the revenue regulations implementing the VAT law* (Rev. Reg. 5-87), *expressly provides that "raw cane sugar" to which VAT exemption is limited does not include molasses, among others."*

*In fine, Rev. Reg. 5-87 merely reiterated the provisions of Sec. 103 of the Tax Code (the act of the legislature/Congress) pertaining to the items exempt from the VAT although they undergo the milling process, raw cane sugar being one of them, and clarified that "raw cane sugar"*

> *does not include molasses. It did not add to nor exceed the limitations set forth by the provisions of the VAT law contrary to your claim.* (See pp. 10 & 11, CTA rec.)

*Consistent with the view and argument raised in its written claim for refund filed with the Bureau of Internal Revenue, petitioner, after receipt of respondent's letter of denial on January 26, 1993, filed his petition for review with this court on February 23, 1993 seeking the refund of the amount of P789.39 paid as VAT on his sale of molasses.*

*Petitioner contends that molasses is an agricultural product in its original state and so, like raw sugar, it is exempt from VAT. He avers that molasses is an intermediary product of a simple operation of milling sugar cane into raw sugar or that it is a by-product of sugar cane in processing the same into sugar. Hence, there is no rhyme or reason why the exemption of raw sugar from VAT should not be extended to molasses as well. In assailing the validity of Revenue Regulations No. 5-87, Sec. 9 (b), which excluded molasses from the exemption, petitioner alleges that the same extended the letter and spirit of the law, thus amounting to an amendment of the same.*

*Petitioner cited the testimonies of his witnesses, Messrs. Vicente G. Castro and Rogelio Covar, who were qualified as experts, that molasses is a by-product in the manufacture of sugar and pointing to the milling operations or manufacturing process of said products.*

*Testimony of*
*Vicente G. Castro:*

Q. *You said that as general manager of the Bicolandia Sugar Development Corporation, one of your responsibilities was in managing the sugar mills operations. Will you please describe to the honorable Court what precisely does the term "milling operations" refer to?*

A. *Milling operation refers to the grinding of the sugar cane brought to the sugar mill, process the juice into sugar. And the sugar that was manufactured from sugar cane is put in bag and this is sold by the particular owners. That is in brief refers to the sugar manufacturing.*

Q. *Will you please inform the court what other product is produced by the same process of milling operations?*

A. *When the sugar cane is grinded and crushed, the juice is clarified. After the juice is clarified, this is boiled. After it has undergone boiling, this will go to the crystallizer whereby the pure sugar is made into crystals. And that component that could not be crystallized goes to the molasses. So in effect, molasses is a by-product of sugar cane in processing the sugar cane into sugar.* (Underlining supplied.)

(pp. 9 & 10, TSN, July 12, 1993.)

*Testimony of*
*Rogelio Covar:*

Q. *Will you please describe to the honorable Court what you meant by sugar mill operations?*

A. *Well, sugar mill operations involve essentially cane processing. At the onset, I wish to inform Your Honors that sugar or raw sugar or sucrose - the chemical substance which is known really as raw sugar - is produced in the sugar cane plant by a process called photosynthesis. And this is stored in the sugar cane cells. This is the sucrose which we seek to crystallize and sell to the public as raw sugar.*

*Now, this is included and contained in the sugar cane stalk which is delivered to the factory for processing. As soon as these cane stalks are delivered to the factory, these are weighed and brought to a conveyor where it is passed through cane knives. And these are cut into small pieces probably one foot length. Once this is cut into these small pieces, this is passed through a crusher. And canes are crushed so that the cells will be destroyed.*

*Now, after crushing, this is passed through a shredder where the fibers are shred so that the juice can be further extracted. From the shredders, this is passed through a series of mill train which we call a mill tandem which consist of four or five sets of rollers.*

*Now, in these rollers, the cane cells are pressed under pressure so that the juice comes out and the fiber content is separated when it passes through the last mill. The fiber content which is separated with the trash is what we call bagasse. Now, this is the first by-product in sugar cane manufacture. The juice which is separated from the bagasse by the extraction is now passed through a clarifier. In the clarifier, lime is added* *together with phosphoric acid so that the dirtier portions of the juice will be separated from the pure juice. Once this is done, then the juice is passed through a series of filters. We call it a rotary drum filter.*

*Now, the clarified juice, after passing through the filter, is sent to the boiler. The thick substance that separates from or the precipitate separating from the filtering is what we call a second by-product which is known as the filter press or mud press. The clear juice once it goes to the boiler is boiled through multiple effect evaporators wherein the water is separated from the pure sucrose.*

*Now, after it has passed through boiling, this goes to a vacuum pan where the thick syrup is further evaporated under pressure so that the sucrose will not caramelize.*

*Now, from there, it is dropped through a crystallizer where the syrup which is now called a massecuite contains molasses and the crystalline sucrose. This is now dropped to a centrifuge wherein the crystal is separated from the viscous liquid known as molasses.*

*Now, these crystallized substance is what we call raw sugar, and the thick viscous liquid which is separated from the massecuite is what we call molasses. And since we have recovered now the pure raw sucrose in crystalline form, the viscous and dirty substance which comes out is known as the molasses and it's a by-product of a sugar manufacture.*

*Now, these crystalline sugar now is dried and placed in bags and sold as raw sugar.*

*Q. So that in your opinion, Mr. Covar, can you tell the court whether molasses can be considered as an agricultural product in its original state?*

> A. *Molasses is considered an agricultural product because, as I have said, there is no change involved, there is no chemical change involved in the process except a physical separation between the crystalline raw sugar which is the major product and molasses which is a by-product.*

(pp. 18 to 23, TSN, July 12, 1993.)

*The Court finds petitioner's view not well taken.*

*"Molasses is the thick, brown or dark-colored, viscid sirup which drains from sugar in the process of manufacture."* **(Webster's International Dictionary,** 2nd Ed., p. 1579.) *From the concept of milling operations or manufacturing process that produce sugar and molasses described by petitioner's expert witnesses, molasses cannot qualify as an agricultural product in its original state because the process of production or manufacture thereof does not merely involve a simple process of preparation or preservation for the market, such as freezing, drying, salting, smoking or stripping as contemplated by law* (Section 103 (b) of the Tax Code as amended) *but one that covers an intricate process and several stages of activities. Truly, the expert witnesses even admit in their testimonies that molasses results from a manufacturing process. Let us*

consider these series of activities that go into the manufacture of sugar and molasses as condensed from the testimony of petitioner's witness Mr. Rogelio Covar:

> Delivery of sugar cane stalks to the factory
>
> Cutting of sugar cane into small pieces
>
> Crushing or grinding the same through a crusher
>
> Shredding through a shredder
>
> Passing through a series of "mill train" or "mill tandem" or "sets of rollers"
>
> Clarifying of crushed sugar cane juice into a clarifier in which lime and phosphoric acid are added to separate pure juice from the dirtier portions of the juice
>
> Passing of the sugar cane juice through a series of filters called "rotary drum filter"
>
> Boiling of clarified juice through a boiler and "multiple effect evaporators", wherein water is separated from the pure sucrose.
>
> Passing of juice to a vacuum pan to further evaporate the thick syrup
>
> Crystallizing of pure sucrose through a crystallizer.
>
> Separating the crystallized sucrose called "raw sugar" from the viscous liquid called "molasses", through a "centrifuge"
>
> Drying of crystalline sugar and placing same in bags for sale.

In fact, in one of the stages of the manufacturing process, that is the stage of clarifying crushed sugar cane juice into a clarifier, lime (a mineral) and phosphoric acid (a chemical) are added or used.

*Such manufacturing process, which molasses undergoes, negates the concept of its being "in its original state" that would qualify it as an agricultural product exempt from VAT under said Section 103 (b) of the Tax Code which provides that agricultural food products should be considered in their original state even if they have undergone the simple processes of preparation or preservation for the market, such as freezing, drying, salting, smoking or stripping. Indeed, prior to the value-added tax provisions in the Internal Revenue Code, the previous percentage tax provisions of said* Code, (Sec. 198 (a) and (b), 1977 Tax Code) *defines even the phrase "whether in their original state or not" as "the transformation of said products by the application of simple processes to preserve or otherwise prepare said products for the market such as freezing, drying, salting, smoking or stripping."*

*Be that as it may, the focal point really in petitioner's position is that since the law* (Section 103 (b) of the Tax Code, *supra) considers raw cane sugar as an agricultural product in its original state and thus exempt from VAT, why should molasses, which undergoes the same milling or* *manufacturing process, be not similarly considered and likewise exempted from VAT?*

*Well, the point is that while molasses has undergone almost the same milling or manufacturing process as raw cane sugar, it is only a by-product. It is not sugar or even similar to it in physical structure and use. And the law considers raw cane sugar, the principal product, together with polished or husked rice and corn grits, as an agricultural product in its original state and does not include molasses as such. On this point, we find the position of respondent in his letter of December 29, 1992 heretofore cited as tenable:*

> *Please be informed that the issue on the taxability of the sale of molasses has been squarely resolved in VAT Ruling No. 058-90 dated February 28, 1990 wherein it was held that -*
>
> > *"Generally, milling which employs technology and machinery, is not considered as a simple process for the purpose of qualifying agricultural products as remaining in their original state. Thus, all milled products with the exception of rice, corn grits and raw cane sugar, are no longer in their original state; hence not exempt from the VAT* (Section 103 (b) of the Tax Code as implemented by Section 9 (b)(2) of Rev. Reg. 5-87). *Molasses, although a by-product of sugar milling, is not however considered as raw cane sugar; hence its sale is subject to 10% VAT pursuant to Section 100 of the same Code."*

*The rule of* **exclusio unius est exclusio alterius**, *contrary to petitioner's postulation, may be applied in this case, there being no positive or strong legislative fiat that would justify the inclusion of molasses in the exemption. Furthermore, exemption from taxation is not favored and should be construed* strictissimi juris *against the taxpayer and liberally in favor of the taxing authority.* **(Philippine Petroleum Corporation vs. Municipality of Pililla, Rizal, 198 SCRA 82; Caltex Philippines, Inc. vs. Commission on Audit, et al., 208 SCRA 726; Commissioner of Internal Revenue vs. Guerrero, 21 SCRA 180; Manila Electric Co. vs. Vera, 67 SCRA 351.)**

*Verily, Section 9 (b) of Revenue Regulations No. 5-87 which implements the VAT provisions in question, is valid and correct. Said regulations, in stating that molasses is not included in the exemption, merely upholds Sec. 105 (b) of the NIRC which itself does not include or consider molasses as an agricultural product in its original state and thus, unlike raw cane sugar, is exempt from VAT. In other words, Section 9 (b) of Revenue Regulations No. 5-87 is in accordance with law and does not extend nor amend the provisions of Section 103 (b) of the Tax Code. Again, we agree with respondent's stand on this matter:*

> *In fine, Rev. Reg. 5-87 merely reiterated the provisions of Sec. 103 of the Tax Code (the act of the legislature/Congress) pertaining to the items exempt from the VAT although they undergo the milling process, raw cane sugar being one of them, and clarified that "raw cane sugar" does not include molasses. It did not add to nor exceed the limitations set forth by the provisions of the VAT law contrary to your claim.* (See pp. 10 & 11, CTA rec.)

*Petitioner has invoked some jurisprudence on the term agricultural products whether or not in their original state as exempt from percentage tax or sales tax under the old percentage tax provisions of the Tax Code. But what he failed to notice is that those doctrines relate to other agricultural food and non-food products whether in their original state or not under the old provisions of the Tax Code which have undergone revisions. And that, under the later editions of the National Internal Revenue Code* (NIRC of 1977 & NIRC as revised in 1987) *the phrase "whether in their original state or not" qualifying agricultural products, refers to those which have simply undergone the simple process of preparation or preservation. Never in the history of the pertinent Tax Code provisions nor by jurisprudence has molasses been considered as an agricultural food product in its original state and therefore* exempt even from percentage tax or sales tax then enforced.

WHEREFORE, petitioner's petition for review is not sustained and his claim for refund therein sought for, is DENIED.

SO ORDERED.

RAMON O. DE VEYRA
Associate Judge

WE CONCUR:

ERNESTO D. ACOSTA
Presiding Judge

MANUEL K. GRUBA
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