REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

ATLAS CONSOLIDATED MINING AND DEVELOPMENT CORPORATION,
Petitioner,

- versus -

C.T.A. CASE NO. 4264

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

x - - - - - - - - - - - x

5/13/93

D E C I S I O N

This case stems from an assessment issued against petitioner for deficiency ad valorem tax, plus surcharge aggregating P1,059,063.47 for the year 1977 and for deficiency income taxes for 1977 and 1978 including interest in the amounts of P883,460.76 and P16,937.51 respectively.

Petitioner is a domestic corporation organized and existing under and by virtue of the laws of the Republic of the Philippines and is engaged primarily in the business of mining copper.

On April 15, 1983, respondent issued against petitioner the subject assessments which was seasonably contested on April 27, 1983 (BIR records, p. 123).

On April 14, 1988, respondent denied the protests by issuing and serving upon the petitioner warrants of distraint and levy (Annexes A and B) which later on was lifted upon petitioner's filing of a surety bond in the amount of P3,640,831.61 (BIR records, p. 224).

Hence, this petition for review.

During the course of the proceedings, the assessment for deficiency income tax became the subject of a compromise settlement which was noted by this Court in its Resolution, dated October 10, 1990 (p. 58, CTA records). Hence, the only remaining issue is the assessment for deficiency ad valorem tax.

Pursuant to a Letter of Authority No. 14561 NA, dated April 30, 1981, revenue examiners of herein respondent conducted an investigation which yielded, among others, the following results:

> "Subject taxpayer is a domestic corporation engaged in mining with copper, gold, silver, pyrite and molybdenum as its main mineral products. Gold is subject to 1 1/2% ad valorem tax (royalty) while the rest at 2% of the actual market value of the gross output. (Sec. 254, par. (b)(2) and (3), NIRC). However, Atlas Consolidated Mining & Development Corporation enjoys certain tax incentives as a non-pioneer industry

in the production of copper, gold and silver.

Verification disclosed that its books of accounts and other related records are being kept and maintained in accordance with the National Internal Revenue Code and the various rules and regulations supplementing and implementing the same.

In the course of investigation, the following assessments were arrived at: (Please see attached working papers for computation and details.)

	1977	1978	Total
Def. Income tax	P857,919.50	P 16,939.72	P 874,859.22
Def. Ad Valorem Tax	-	1,059,063.47	1,059,063.47
Total	P857,919.50	P1,076,003.19	P1,916,922.69

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xxx xxx xxx

xxx xxx xxx

2. Deficiency Ad Valorem Taxes - The deficiency assessment on ad valorem tax for 1978 which is shown below and detailed in the attached working paper was due to the quantity deductions from the 'final assay for settlement'.

Kind of Metals	1978
Copper	P 695,427.05
Gold	91,103.92
Silver	60,719.81
Sub-total	P 847,250.78
Add: 25% Surcharge	211,812.69
Def. Ad Valorem Tax	P1,059,063.47

The following facts and arguments were presented to the taxpayer's representative to support the deficiency assessments:

> 1) That the copper concentrates were shipped to the smelters/buyers abroad, namely "MITSUBISHI METAL CORPORATION", MARCK RICH & CO. and PHILIPP BROTHERS OCEANIC, INC.;
>
> 2) That the ad valorem taxes paid were based on the provisional assay at the prevailing price of the metals at the London Metal Exchange Quotation;
>
> 3) That when the copper concentrates reached the smelter abroad, the provisional assay is redetermined by the assayers of the seller and buyer in order to arrive at a "Final Assay for settlement." The final assay for settlement is the stage where the sale is perfected, meaning the seller has to part with the ownership of the goods and the buyer is bound to pay for the price. In some instance, if the assayers of both parties could not agree on the "final assay for settlement," the difference is settled by a third party called the umpire assayer; and
>
> 4) That in the shipments made in 1978, <u>certain units or percentage were deducted from the final assay for settlement resulting in the understatement of the actual market value of the metals subject to ad valorem tax</u>." (Underscoring supplied)
>
> (BIR Investigation Report dated Feb. 8, 1983, pp. 96-97, BIR records.)

In the BIR Assessment Demand Letter of April 15, 1983, however, the Acting Commissioner at that time informed the petitioner that "no deficiency business tax was found due from you for the year 1977" (Exhibit A, p. 70, CTA records) but:

> "the same investigation also disclosed that there is due from you for the year

> 1978 the amount of P1,059,063.43 as deficiency ad valorem tax and surcharge, computed as follows:
>
> | | Understatement of market value of metals per investigation | Ad Valorem Tax |
> |---|---|---|
> | Copper | P34,771,352.43 | P695,427.05 |
> | Gold | 6,073,594.35 | 91,103.92 |
> | Silver | 3,035,990.55 | 60,719.81 |
> | Total | | P847,250.78 |
> | Add: 25% surcharge | | 211,812.69 |
> | TOTAL AMOUNT DUE AND COLLECTIBLE | | P1,059,063.47" |
>
> (ibid.)

In other words, the deficiency assessment was arrived at due to petitioner's understatement of the market value of the metals it shipped abroad by deducting certain units or percentage from the quantity of the metals determined in the final assay.

In a letter, dated April 27, 1983, petitioner protested the assessment on the ground that "the practice prevailing in the metals (like copper) world market is to allow the buyer a 'unit deduction' expressed in percentage from the quantity determined in the final assay." (p. 123, BIR records.) This "unit deduction" is unpaid for. The petitioner in the same protest letter explained, thus:

> "Why? Because the smelter/buyer needs to provide for inevitable losses of metal in processing raw copper into refined copper. 'Unit deduction' is the built-in device to correct this loss.

> It is this unpaid for metal content that your examiners would now tax against ACMDC. This is an insult added to injury. The miner, ACMDC not only was not paid for the unit deduction but your Office would punish it with a tax on such unpaid quantity." (ibid.)

Hence, the petitioner believes that it should not be subjected to assessment for deficiency ad valorem taxes.

The only issue, then, is whether or not the assessment for deficiency ad valorem taxes in the amount of P1,059,063.47 including surcharge was valid. More specifically, whether or not the "actual market value of the gross output" under Sec. 254 of the Tax Code (1977) where the ad valorem tax is based, includes the "unit deduction" for taxation purposes.

We submit that both questions should be answered in the negative.

Quoted, hereunder, for easy reference, is the applicable law for the resolution of this case which reads in part:

> "Sec. 254. Rentals and Royalties on Mineral Lands Under Lease.- For the privilege of exploring, developing, mining, extracting, and disposing of the minerals from the lands covered by lease, there is thereby imposed upon the lessee rentals and royalties, as follows:
>
> xxx xxx xxx

> (B) Royalties -
>
> xxx xxx xxx
>
> 2) On gold, a royalty of one and one-half per centum of the actual market value of the annual gross output thereof.
>
> 3) On all other minerals, extracted from, or mineral products of, mineral lands of the first, second, fourth and fifth groups as provided in the Mining Act, a royalty of two per centum of the actual market value of the gross output thereof. (Underscoring supplied.)
>
> xxx xxx xxx
>
> (1977 National Internal Revenue Code)

Sec. 257 of the same Tax Code defines "gross output" as "the actual market value of minerals or mineral products, or of bullion from each mine or mineral lands operated as a separate entity without any deduction from mining, milling, refining, transporting, handling, marketing, or any other expenses".

The nature of ad valorem tax on mining, as ruled by the Supreme Court, is a tax not on the minerals, but upon the privilege of severing or extracting the same from the earth, the Government's right to exact the said impost springing from the Regalian theory of state ownership of its natural resources. **(Cebu**

Portland Cement Co. vs. Comm. of Int. Rev., L-18649, Feb. 27, 1965, 13 SCRA 333.) Since the ad valorem tax is a severance tax, i.e., a charge upon the privilege of severing or extracting minerals from the earth, and is due and payable upon removal of the mineral product from its bed or mine, the tax is to be computed on the basis of the market value of the mineral in its condition at the time of such removal and before its being substantially changed by chemical or manufacturing (as distinguished from purely physical) processing. **(Cebu Portland Cement Co. vs. Comm. of Int. Rev.,** L-18649, Resolution dated Dec. 29, 1967 of the Motion for Reconsideration, 21 SCRA 1425.) It should be noted, however, that in a latter case of similar nature, the Supreme Court delimited the basis for the computation of the ad valorem tax not only on the market value but on the actual market value of the mineral products extracted or produced. **(Republic Cement Corp. vs. Comm. of Int. Rev.,** 23 SCRA 967 [1968].) The "actual market value" of property, for purposes of taxation means the selling price of the article in the course of ordinary business. **(San Miguel Corp. vs. Municipal Council of Mandaue, Cebu,** 52 SCRA 43.) Construed, therefore, the ad valorem tax must be based on the actual market value, i.e., the value after the "unit deduction" from the quantity of the metals determined in the final assay has been applied. The price after the unit deduction is considered the actual market value of the metal. This "unit deduction" is the prevailing practice in the metals world market and is considered as a built-in device for the buyer to provide for inevitable losses of metal in processing raw copper into refined copper. This is expressed in percentage from the quantity determined in the final assay. This practice is normal and ordinary in the metals sales contracts executed by exporters and buyers. To go against this practice means to put an end to the petitioner's business since it cannot find buyers for its copper. And one cannot speak of "actual market value" when there are no buyers in the course of ordinary business. This is one of the peculiar realities of the world metals market. Thus, if it is determined in the final assay that the copper concentrate exported in a particular shipment contained 28% metal, then the buyer paid for only 27%. The 27% is now the "actual market value" of the "gross output" from where the ad valorem tax should be based. This, We believe, is the intent of Sec. 254 of the Tax Code (1977). A contrary interpretation will only lead to injustice and inequity.

WHEREFORE, premises considered, the subject assessment for deficiency ad valorem tax against petitioner is hereby declared null and void.

SO ORDERED.

Quezon City, Metro Manila, May 13, 1993.

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