REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

EN BANC

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COMMISSIONER OF INTERNAL REVENUE, Petitioner,	**CTA EB No. 1918** (CTA Case No. 9123)
	Present:
- versus -	**DEL ROSARIO**, P.J., **CASTAÑEDA, JR.**, **UY**, **FABON-VICTORINO**, **MINDARO-GRULLA**, **RINGPIS-LIBAN**, **MANAHAN**, **BACORRO-VILLENA**, and **MODESTO-SAN PEDRO**, JJ.
PHILIPPINE INTERNATIONAL AIR TERMINALS CO. INC., Respondent.	***Promulgated:*** JUN 03 2020 3:15 p.m.

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DECISION

UY, J.:

The instant *Petition for Review*[1] filed on August 31, 2018 by the Commissioner of Internal Revenue, petitioner, against Philippine International Air Terminals Co., Inc., respondent, prays for a reconsideration and setting aside of the Decision dated May 7, 2018 and Resolution dated July 27, 2018, promulgated by the Third Division of this Court in CTA Case No. 9123, entitled *"Philippine International Air Terminals Co., Inc., Petitioner, vs. Commissioner of Internal Revenue, Respondent,"* the dispositive portions of which respectively read as follows:

[1] EB Docket, pp. 5 to 18.

Decision dated May 7, 2018:

> "**WHEREFORE,** premises considered, judgment is rendered as follows:
>
> 1) **GRANTING** the instant Petition for Review and **SETTING ASIDE** and **CANCELLING** the three (3) Final Decision on Disputed Assessment all dated July 14, 2015 for taxable years 2000, 2001 and 2002 issued by Respondent Commissioner of Internal Revenue for lack of merit;
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> 2) **CONFIRMING** Petitioner's entitlement to incentives under R.A. No. 9716[2], particularly its exemption from VAT; and
>
> 3) **DECLARING** that Petitioner is not liable for any deficiency VAT for taxable years 2000, 2001 and 2002.
>
> **SO ORDERED.**"

Resolution dated July 27, 2018:

> "**WHEREFORE,** premises considered, Respondent's 'Motion for Reconsideration' filed on May 24, 2018 *via* registered mail is **DENIED** for lack of merit.
>
> Likewise, Petitioner's 'Manifestation' is **NOTED.**
>
> **SO ORDERED.**"

THE FACTS

Petitioner CIR is the duly appointed Commissioner of the Bureau of Internal Revenue (BIR), who has the power to decide disputed assessments, refunds of internal revenue taxes, fees or other charges, penalties imposed in relation thereto or other matters arising under the National Internal Revenue Code (NIRC) of 1997, as amended, or other laws or portions thereof administered by the BIR. He holds office at the BIR National Office Building, Agham Road, Diliman, Quezon City.

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[2] Should be R.A. 7916 - "The Special Economic Zone Act of 1995".

Respondent Philippine International Air Terminals Co., Inc. (PIATCO) is a domestic corporation duly organized and existing under Philippine laws, with principal office at the 3rd Floor, PAIR-PAGS Center, Ninoy Aquino International Airport ("NAIA") Compound, NAIA Avenue, Pasay City.

In 1998, PIATCO registered with the Philippine Export Zone Authority (PEZA) as an "Ecozone Developer/Operator" to "establish, develop, construct, administer, manage and operate a special economic zone to be known as PIATCO Special Economic Zone."

PIATCO also registered with the PEZA as an "Economic Zone Facilities Enterprise" to "engage in the construction and operation of the NAIA Terminal Passenger 3 at the PIATCO Special Economic Zone."

In a Letter dated June 17, 1998, PIATCO formally notified the PEZA that it was waiving the income tax holiday incentives granted under Executive Order (E.O.) No. 226. In view of this waiver, Petitioner was entitled to "exemptions from all national and local taxes."

On June 24, 2002, PIATCO received from the CIR, Letter of Authority (LOA) No. 0029367 dated June 20, 2002 ("First LOA"), informing PIATCO that BIR examiners were authorized to examine its books of account and other accounting records "for all internal revenue taxes for the period from January 01, 1997 to December 31, 2001."

On November 04, 2003, after several conferences with the BIR, PIATCO received an undated Preliminary Assessment Notice ("First PAN"). On November 19, 2003, PIATCO submitted its written reply to the First PAN.

On April 17, 2006, PIATCO received a Formal Letter of Demand dated 15 January 2006 ("First FLD"), with seventeen (17) Assessment Notices all dated April 07, 2006, demanding payment of deficiency taxes, including VAT, for taxable years 1997 to 2001. On May 17, 2006, PIATCO filed with the CIR its Protest Letter against the First FLD.

On February 09, 2007, the CIR issued an FDDA ("First FDDA") finding PIATCO liable for deficiency taxes in the total amount of ₱24,423,565.09 for taxable years 1997 to 2001.

On February 14, 2007, PIATCO remitted payments to the CIR for deficiency taxes covering taxable years 1997 to 2001 in the amount of ₱24,423,565.09, in compliance with the First FDDA.

On September 30, 2008, PIATCO received: (a) BIR LOA No. 000044211 dated September 18, 2008 ("Second LOA") for the examination of PIATCO's deficiency VAT for taxable year 2001, and (b) Notice of Informal Conference dated September 26, 2008 to be held on October 03, 2008.

On January 12, 2009, PIATCO received: (a) BIR LOA No. 00006822 dated December 10, 2008 ("Third LOA") for the examination of deficiency VAT on importations for taxable year 2000, and a Notice of Informal Conference dated January 08, 2009 to be held on January 14, 2009, and (b) BIR LOA No. 00006821 dated December 10, 2008 ("Fourth LOA") for the examination of deficiency VAT on importations for taxable year 2002, and a Notice of Informal Conference dated January 08, 2009 to be held on January 14, 2009.

In its initial findings, the CIR assessed PIATCO the following: (a) ₱51,406,057.47 as deficiency VAT for taxable year 2000, (b) ₱682,927,427.37 as deficiency VAT for taxable year 2001 and (c) ₱475,914,313.89 as deficiency VAT for taxable year 2002, inclusive of surcharge and interest. The alleged deficiency VAT assessments all pertain to PIATCO's importations of capital equipment, building materials and supplies used in the construction of the NAIA Passenger Terminal 3 facilities.

After the informal conferences, the CIR issued to PIATCO three (3) PANs dated: (a) January 23, 2009 assessing deficiency VAT for taxable year 2001 in the amount of ₱698,710,054.48 ("Second PAN"), (b) March 16, 2009 assessing deficiency VAT for taxable year 2000 in the amount of ₱51,976,782.93 ("Third PAN") and (c) March 16, 2009 assessing deficiency VAT for taxable year 2002 in the amount of ₱477,161,015.16 ("Fourth PAN"). The deficiency VAT assessments all pertain to PIATCO's importations under its PEZA registrations.

On February 27, 2009 and April 03, 2009, PIATCO filed its letter replies to the Second PAN, Third PAN and Fourth PAN.

In response, on August 08, 2012, the CIR sent a letter to PIATCO with the attached BIR Memorandum dated July 24, 2012 issued by BIR Region No. 8, declaring that PIATCO's importations of construction materials and equipment under its PEZA registrations are exempt from VAT, and as such, the proposed 2000 to 2002 deficiency VAT assessments are null and void for lack of legal basis, considering the case closed and terminated.

On February 23, 2015, notwithstanding the previous letter of the CIR dated August 08, 2012, PIATCO received FANs all dated February 23, 2015 assessing the same deficiency VAT for TY 2000, 2001 and 2002. On March 25, 2015, PIATCO filed its protest against the FANs.

On July 20, 2015, PIATCO received from the CIR three (3) FDDA dated July 14, 2015 upholding PIATCO's liability for deficiency VAT amounting to (a) ₱73,057,388.40 for taxable year 2000 ("Second FDDA"), (b) ₱1,012,652,812.14 for taxable year 2001 ("Third FDDA") and ₱698,994,433.69 for taxable year 2002 ("Fourth FDDA").

Consequently, PIATCO filed a Petition for Review on August 19, 2015 before the Court in Division docketed as CTA Case No. 9123.

On September 18, 2015, PIATCO received from the CIR three (3) Final Notices before Seizure ("the Notices") dated September 18, 2015. Therein, the CIR demanded payment of VAT liabilities for taxable years 2000, 2001 and 2002 in the total amount of ₱2,263,152,164.26 including penalties, surcharge and interest. PIATCO was informed in the Notices that in case of failure to pay the amounts assessed as deficiency VAT, the CIR would serve and execute the Warrant of Distraint and/or Levy and Garnishment already prepared to enforce collection.

In response to the Notices, PIATCO filed a Motion for Suspension of Collection of Tax on September 28, 2015, praying that the Court in Division issue an Order directing the CIR to withdraw the Notices and suspend all acts to collect tax deficiencies from PIATCO, including the issuance of a Warrant of Distraint and/or Levy and Garnishment. PIATCO also prayed for the posting of a surety bond in an amount lower than the principal amount of the deficiency VAT of ₱430,463,290.23. *ro*

On September 30, 2015, PIATCO filed its Supplemental Motion for Suspension of Collection of Tax, praying that a Writ of Preliminary Injunction be issued without need of posting a bond, and if a bond was needed that it be an amount substantially lower than the basic tax assessed.

In the Answer[3] filed in CTA Case No. 9123 on October 23, 2015, the CIR interposed the following special and affirmative defenses: PIATCO's importation of capital equipment and construction materials are not exempt from VAT; the BIR's right to assess PIATCO of its deficiency VAT for taxable years 2000, 2001, and 2002, is not barred by prescription; and the BIR can still assess PIATCO for deficiency VAT for taxable years 2000 and 2001, notwithstanding previous investigation and assessment for the same periods.

On November 09, 2015, PIATCO filed its Reply[4] to the CIR's Answer in CTA Case No. 9123 alleging, among others, that PIATCO, as a PEZA registered enterprise, was entitled to fiscal incentives under the Special Economic Zone Act of 1995; and that PIATCO was not estopped from raising the defense of exemption from all internal revenue taxes when it paid deficiency withholding taxes for taxable years 1997 to 2001. PIATCO points out that as there was no falsity or fraud in the returns of PIATCO, the period for respondent to assess deficiency VAT against PIATCO for taxable year 2000, 2001 and 2002 had already prescribed.

On November 27, 2015, PIATCO received the Resolution dated November 25, 2015[5] in CTA Case No. 9123 resolving PIATCO's Motion for Suspension of Collection of Tax filed on September 28, 2015 and Supplemental Motion for Suspension of Collection of Tax filed on September 30, 2015, wherein the Court in Division ruled as follows:

a) Denying PIATCO's Motion for Suspension of Collection of Tax and Supplemental Motion for Suspension of Collection of Tax for being premature; and

b) Putting the CIR on notice that his Civil Remedies for Collection of Taxes under the Tax Code has not yet ripened. Thus, any effort to collect the disputed assessment in the

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[3] Div. Docket, CTA Case No. 9123, Vol. II, pp. 913-920
[4] Div. Docket, CTA Case No. 9123, Vol. II, pp. 922-936
[5] Div. Docket, CTA Case No. 9123, Vol. II, pp. 938-942

basic amount of ₱430,463,290.23 should only be done after a final and executory Decision in this case, provided such is favorable to the CIR.

After the Pre-Trial Conference held on September 6, 2016,[6] the parties filed their Joint Stipulation of Facts and Simplification of Issues[7] on September 16, 2016. Thereafter, the Court in Division issued the Pre-Trial Order dated October 4, 2016[8], approving and adopting the Joint Stipulation of Facts and Simplification of Issues filed by the parties.

During trial, PIATCO presented its witness, Atty. Moises S. Tolentino, Jr. on May 23, 2017. Thereafter, the Court in Division admitted petitioner's formally offered evidence.

On the other hand, counsel for the CIR manifested during the hearing held on August 07, 2017, that he has no witness to present but he will file respondent's Formal Offer of Evidence. Thus, on September 14, 2017, the CIR filed his Formal Offer of Evidence.

On January 12, 2018, the Court in Division issued a Resolution, admitting the CIR's exhibits and directed the filing of parties' respective Memoranda[9]. On February 23, 2018, PIATCO filed its Memorandum[10], while CIR failed to file his Memorandum.[11]

On March 13, 2018, the case was submitted for decision.

In the assailed Decision[12] dated May 7, 2018, the Court in Division granted PIATCO's Petition for Review, set aside and cancelled the three (3) Final Decision on Disputed Assessment all dated July 14, 2015 for taxable years 2000, 2001 and 2002 issued by the CIR for lack of merit. It also confirmed PIATCO's entitlement to incentives under R.A. No. 7916, particularly its exemption from VAT; and declared that PIATCO is not liable for deficiency VAT for the years 2000, 2001 and 2002.

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[6] Minutes of Hearing, September 6, 2016, Div. Docket, CTA Case No. 9123, Vol. III, p.1415
[7] Div. Docket, CTA Case No. 9123, Vol. III, pp. 1419-1426
[8] Div. Docket, CTA Case No. 9123, Vol. II, pp. 1428-1440
[9] Div. Docket, CTA Case No. 9123, Vol. V. pp. 2169-2172
[10] Div. Docket, CTA Case No. 9123, Vol. V. pp. 2173-2215
[11] Records Verification dated February 26, 2019, Div. Docket, CTA Case No. 9123, Vol. V, p. 2216
[12] EB Docket, pp. 19 to 44.

Aggrieved, the CIR filed his *Motion for Reconsideration* on May 24, 2018, to which PIATCO filed its *Comment (to Respondent's Motion for Reconsideration dated 23 May 2018)"* on July 18, 2018. In the assailed Resolution dated July 27, 2018, the Court in Division denied the CIR's *Motion for Reconsideration* for lack of merit.[13]

Undaunted, the CIR filed a *Motion for Extension of Time to File Petition for Review* on August 16, 2018.[14] In the Minute Resolution[15] dated September 6, 2018, the *Motion for Extension of Time to File Petition for Review* was deemed granted, in view of the filing of the Petition for Review by the CIR by registered mail on August 31, 2018.

Thereafter, the CIR filed the instant *Petition for Review* on August 31, 2018.[16]

In the Resolution dated September 19, 2018, PIATCO was ordered to file its Comment within ten (10) days from notice.[17] PIATCO filed a *Motion for Extension of Time*[18] on October 12, 2018, praying for an additional period of fifteen (15) days from October 13, 2018, or until October 28, 2018, within which to file its comment and/or Opposition to the Petition for Review, which was granted by the Court *En Banc* on October 16, 2018.[19]

On October 26, 2018, PIATCO filed its *Comment (to the Commissioner of Internal Revenue's Petition for Review dated 31 August 2018).*[20]

Thereafter, the Court resolved to give due course to the Petition for Review, and directed the parties to file their respective memoranda within thirty (30) days from notice.[21] PIATCO filed its *Memorandum*[22] on February 14, 2019, while Records Verification[23] dated February 28, 2019 shows that the CIR failed to file his Memorandum, despite due notice.

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[13] EB Docket, pp. 45 to 48.
[14] EB Docket, pp. 1 to 3.
[15] EB Docket, p. 59.
[16] EB Docket, pp. 5 to 18.
[17] EB Docket, pp. 61 to 62.
[18] EB Docket, pp. 63 to 66.
[19] EB Docket, p. 67.
[20] EB Docket, pp. 68 to 97.
[21] EB Docket, pp. 104 to 105.
[22] EB Docket, pp. 111 to 143.
[23] EB Docket, p. 144.

In the Resolution dated March 28, 2019, this case was submitted for decision.[24]

Hence, this Decision.

ISSUES

The CIR raises the following grounds for the allowance of his Petition for Review, to wit:

> "(1) THE THIRD DIVISION OF THE HONORABLE COURT ERRED IN HOLDING THAT PIATCO IS EXEMPT FROM VAT ON ITS IMPORTATIONS OF CONSTRUCTION MATERIALS AND EQUIPMENT.
>
> (a) PEZA-registered enterprise's incentive or tax exemption is not absolute. It is subject to the rules and regulations of PEZA, and to the conditions set in its Registration Agreement;
>
> (b) Because of the denial by PEZA of PIATCO's request for tax exemption and duty-free importations of its construction materials and equipment, the aforesaid importations are subject to VAT;
>
> (2) THE THIRD DIVISION OF THE HONORABLE COURT ERRED IN HOLDING THAT PETITIONER'S RIGHT TO ASSESS RESPONDENT PIATCO FOR THE VAT DEFICIENCIES FOR TAXABLE YEARS 2000, 2001 AND 2002 HAD ALREADY PRESCRIBED.
>
> (a) PIATCO admitted that it failed to report in its VAT returns for the period covered the importation of the construction materials and equipment;
>
> (b) For failure to report in its VAT returns the importations for the period covered, PIATCO's VAT returns for the years 2000, 2001 and 2002 are considered false returns that warrants the application of the ten-year period to make an assessment;
>
> (3) THE THIRD DIVISION OF THE HONORABLE COURT ERRED IN HOLDING THAT PETITIONER IS BARRED FROM ASSESSING PIATCO AGAIN FOR

[24] EB Docket, pp. 146 to 147.

> TAXABLE YEARS 2000 AND 2001 IN VIEW OF THE PREVIOUS ASSESSMENTS MADE.
>
> (a) The 'one-examination per year rule' does not apply in cases (sic) fraud, irregularity, or mistakes;
>
> (b) PIATCO committed fraud, irregularity and mistakes in not declaring its importation for VAT purposes despite ruling by PEZA that it is not entitled to avail of duties and tax exemption on its importation of construction materials and equipment;
>
> (c) Finally, the 'one-examination per year rule' under Section 235 of the NIRC, as amended, applies only for income tax purposes and not for VAT purposes as in the case at bar."[25]

Petitioner's arguments:

Petitioner contends that PEZA-registered enterprise's tax incentive or tax exemption is not absolute. It is subject to the rules and regulations of PEZA, and to the conditions set in its Registration Agreement. Because of the denial by PEZA of PIATCO's request for tax exemption and duty-free importation of its construction materials and equipment, the aforesaid importation is subject to VAT.

According to petitioner, PIATCO's VAT returns for the years 2000, 2001 and 2002 are false, thus, warrants the application of the ten-year period to make an assessment. Thus, the BIR is not barred from assessing PIATCO for taxable years 2000 and 2001, notwithstanding previous assessments for the same years.

Respondent's counter-arguments:

Respondent counters that the grounds presented by the CIR in his Petition for Review are mere rehash of arguments already ruled upon by the Court in Division. The CIR allegedly failed to present any compelling evidence or raise any new argument that would merit the reversal of the assailed Decision and Resolution of the Court in Division.

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[25] EB Docket, pp. 9 to 10. mb

Respondent likewise contends that the Court in Division correctly ruled that PIATCO is exempt from VAT on its importations of its construction materials and equipment. PIATCO, as a PEZA-registered entity, is entitled to the fiscal incentives granted under R.A. No. 7916.

In addition, respondent avers that the CIR's right to assess PIATCO for alleged VAT deficiencies for taxable years 2000, 2001, and 2002 had already prescribed.

Finally, respondent argues that the BIR is barred from assessing PIATCO again for taxable years 2000 and 2001, due to its previous assessments.

THE COURT *EN BANC*'S RULING

The instant *Petition for Review* lacks merit.

PIATCO, as a PEZA-registered enterprise, is a VAT-exempt entity, pursuant to Section 8 of R.A. No. 7916, as amended by R.A. No. 8748, which establishes the fiction that Ecozones are foreign territory.

In the subject deficiency VAT assessments issued against respondent PIATCO, petitioner cites as his basis, Section 107 (A)[26] of the NIRC of 1997, as amended, as stated in the PAN dated January 23, 2009,[27] PANs dated March 16, 2009,[28] FANs dated February 23, 2015,[29] and FDDA dated July 14, 2015.[30] According to petitioner,

[26] "**SEC. 107.** ***Value-Added Tax on Importation of Goods***. –
(A) *In General.* – There shall be levied, assessed and collected on every importation of goods a value-added tax equivalent to ten percent (10%) based on the total value used by the Bureau of Customs in determining tariff and customs duties, plus customs duties, excise taxes, if any, and other charges, such tax to be paid by the importer prior to the release of such goods from customs custody x x x."
[27] Exhibit "P-12," Division Docket (CTA Case No. 9123), Vol. 4, pp. 1700 to 1707.
[28] Exhibits "P-13" and "P-14," Division Docket (CTA Case No. 9123), Vol. 4, pp. 1708 to 1722.
[29] Exhibits "P-19" and "P-20," Division Docket (CTA Case No. 9123), Vol. 4, pp. 1846 to 1857.
[30] Exhibits "P-23" to "P-23-7," "P-24" to "P-24-7," "P-25" to "P-25-4," Division Docket (CTA Case No. 9123), Vol. 4, pp. 1985 to 1992, and Vol. 5, pp. 2004 to 2011, and 2023 to 2027.

respondent PIATCO is not a VAT-exempt entity, and should be held liable for deficiency VAT on its importations of construction materials and equipment.

We disagree.

R.A. No. 7916, as amended by R.A. No. 8748, otherwise known as the "The Special Economic Zone Act of 1995," was enacted by Congress, with the goal of attracting legitimate and productive foreign investments, through the establishment of special economic zones, as stated in Sections 2 and 3 thereof, to wit:

> "**SEC. 2.** *Declaration of Policy.* – It is the declared policy of the government to translate into practical realities the following State policies and mandates in the 1987 Constitution, namely:
>
> (a) The State recognizes the indispensable role of the private sector, encourages private enterprise, and provides incentives to needed investments." (Sec. 20, Art II)
>
> (b) The State shall promote the preferential use of Filipino labor, domestic materials and locally produced goods and adopt measures that help make them competitive. (Sec. 12, Art XII)
>
> In pursuance of these policies, the government shall actively encourage, promote, induce and accelerate a sound and balanced industrial, economic and social development of the country in order to provide jobs to the people specially those in the rural areas, increase their productivity and their individual and family income, and thereby improve the level and quality of their living condition through the establishment, among others, of special economic zones in suitable and strategic locations in the country and through measures that shall effectively attract legitimate and productive foreign investments.
>
> **SEC. 3.** *Purposes, Intents and Objectives.* – It is the purpose, intent and objective of this Act:
>
> (a) To establish the legal framework and mechanisms for the integration, coordination, planning and monitoring of special economic zones, industrial

estates / parks, export processing zones and other economic zones;

(b) To transform selected areas in the country into highly developed agro industrial, industrial, commercial, tourist, banking, investment, and financial centers, where highly trained workers and efficient services will be available to commercial enterprises;

(c) To promote the flow of investors, both foreign and local, into special economic zones which would generate employment opportunities and establish backward and forward linkages among industries in and around the economic zones;

(d) To stimulate the repatriation of Filipino capital by providing attractive climate and incentives for business activity;

(e) To promote financial and industrial cooperation between the Philippines and industrialized countries through technology-intensive industries that will modernize the country's industrial sector and improve productivity levels by utilizing new technological and managerial know-how; and

(f) To vest the special economic zones on certain areas thereof with the status of a separate customs territory within the framework of the Constitution and the national sovereignty and territorial integrity of the Philippines."

In pursuit of the foregoing objectives, Congress resolved to accord special economic zones with the status of a **<u>separate customs territory</u>**, as stated in Section 8 of R.A. No. 7916, as amended, to wit:

"**SEC. 8**. *ECOZONE to be Operated and Managed as Separate Customs Territory.* – The ECOZONE shall be managed and operated by the PEZA as separate customs territory.

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The designation of the ecozone as a separate customs territory, means that "in such zone is created the legal fiction of **foreign territory**."[31] Thus, while "an ecozone is indubitably a geographical territory of the Philippines, it is however, regarded in law as **foreign soil**. This legal fiction is necessary to give meaningful effect to the policies of the special law creating the zone."[32]

The foregoing categorization of an ecozone as foreign territory, finds relevance in taxation, particularly in the VAT system, as the Philippines adheres to the ***Cross Border Doctrine,*** which states that "no VAT shall be imposed to form part of the cost of goods destined for consumption outside of the territorial border of the taxing authority."[33]

In other words, importations made into Philippines customs territory are subject to Philippine customs and tax laws, such as VAT, which is a tax on consumption levied on the importation of goods into the Philippines.[34] On the other hand, importations into ecozones are considered importations made into foreign territory, and are *not* subject to VAT.

Correspondingly, importations made by PEZA-registered enterprises, which are located in ecozones considered as foreign territory, are not subject to VAT. In fact, in the case of *Commissioner of Internal Revenue vs. Toshiba Information Equipment (Phils.), Inc.,*[35] the Supreme Court categorically declared that PEZA-registered enterprises are VAT-exempt entities, by virtue of the fiction that ecozones are considered foreign territory, to wit:

> "This Court agrees, however, that **PEZA-registered enterprises, which would necessarily be located within ECOZONES, are VAT-exempt entities, *not* because of Section 24 of Rep. Act No. 7916, as amended, which imposes the five percent (5%) preferential tax rate on gross income of PEZA-registered enterprises, in lieu of all taxes; but, rather, because of Section 8 of the same statute which**

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[31] *Commissioner of Internal Revenue vs. Seagate Technology (Philippines),* G.R. No. 153866, February 11, 2005.
[32] *Id.*
[33] *Coral Bay Nickel Corporation vs. Commissioner of Internal Revenue,* G.R. No. 190506, June 13, 2016.
[34] Sections 4.105-2 and 4.107-1, Revenue Regulations No. 16-2005.
[35] G.R. No. 150154, August 9, 2005.

establishes the fiction that ECOZONES are foreign territory.

It is important to note herein that respondent Toshiba is located within an ECOZONE. An ECOZONE or a Special Economic Zone has been described as —

> ...[S]elected areas with highly developed or which have the potential to be developed into agro-industrial, industrial, tourist, recreational, commercial, banking, investment and financial centers whose metes and bounds are fixed or delimited by Presidential Proclamations. An ECOZONE may contain any or all of the following: industrial estates (IEs), export processing zones (EPZs), free trade zones and tourist/recreational centers.

The national territory of the Philippines outside of the proclaimed borders of the ECOZONE shall be referred to as the Customs Territory.

Section 8 of Rep. Act No. 7916, as amended, mandates that the PEZA shall manage and operate the ECOZONES as a separate customs territory; thus, creating the fiction that the ECOZONE is a foreign territory. As a result, sales made by a supplier in the Customs Territory to a purchaser in the ECOZONE shall be treated as an exportation from the Customs Territory. Conversely, sales made by a supplier from the ECOZONE to a purchaser in the Customs Territory shall be considered as an importation into the Customs Territory.

Given the preceding discussion, what would be the VAT implication of sales made by a supplier from the Customs Territory to an ECOZONE enterprise?

The Philippine VAT system adheres to the ***Cross Border Doctrine***, according to which, no VAT shall be imposed to form part of the cost of goods destined for consumption outside of the territorial border of the taxing authority. Hence, actual export of goods and services

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from the Philippines to a foreign country must be free of VAT; while, those destined for use or consumption within the Philippines shall be imposed with ten percent (10%) VAT." *(Emphasis supplied.)*

In this case, respondent PIATCO was able to prove that it was a PEZA-registered entity, having presented the following: 1) Certificate of Registration No. EZ-98-01,[36] to prove that it is duly registered as an "Ecozone Developer/Operator"[37]; and 2) Certificate of Registration No. 98-01-F,[38] showing that it is duly registered as an "Ecozone Facilities Enterprise."[39]

Accordingly, as a PEZA-registered entity, respondent PIATCO is considered a VAT-exempt entity, because of Section 8 of R.A. No. 7916, establishing the fiction that ecozones are foreign territory. Thus, the importations made by PIATCO into the ecozones are

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[36] Exhibit "P-26," Division Docket (CTA Case No. 9123), Vol. 5, pp. 2039 to 2049.

[37] *Rules and Regulations to Implement Republic Act No. 7916*, **SECTION 2.** Definition of Terms - For purposes of these Rules and Regulations, the following definitions shall apply:
xxx xxx xxx

o. "*ECOZONE Developer/Operator*" refers to a business entity or concern duly registered with and / or licensed by the PEZA to develop, operate and maintain an ECOZONE or nay or all of the component IE, EPZ, Free Trade Zone or Tourist / Recreational Center and the required infrastructure facilities and utilities such as light and power system, water supply and distribution system, sewerage and drainage system, pollution control devices, communication facilities, paved road network, administration building and other facilities as may be required by the PEZA. The term shall include the PEZA and / or the Local Government Unit when by the themselves or in joint venture with a qualified private entity, shall act as the Developer / Operator of the ECOZONES. As such, they shall be entitled to the same incentives under Rule XIV of these Rules in accordance with the pertinent provisions of the Act and the Code.

[38] Exhibit "P-27," Division Docket (CTA Case No. 9123), Vol. 5, pp. 2050 to 2057.

[39] *Rules and Regulations to Implement Republic Act No. 7916*, **SECTION 2.** Definition of Terms - For purposes of these Rules and Regulations, the following definitions shall apply:
xxx xxx xxx

n. "*ECOZONE Facilities Enterprise*" shall refers to a business entity or concern within the ECOZONE duly registered with and / or franchised / licensed by the PEZA with or without incentives provided under Republic Act No. 6957, as amended, (the Build-Operate-Transfer Law) and / or with or without financial exposure on the part of the PEZA such as contractors / operators of buildings, structures, warehouses, site development and road network, ports, sewerage and drainage system and other facilities for the development, operation and maintenance of the ECOZONE and other similar or ancillary activities as may be determined by Board.

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considered importations made into foreign territory, and are not subject to VAT.

PIATCO, as a PEZA-registered entity, is likewise entitled to exemption from national and local taxes, pursuant to Section 24 of R.A. No. 7916, as amended by R.A. No. 8748.

In addition to being considered as VAT-exempt entities because they operate in ecozones that are treated as separate customs territories, it should be emphasized that PEZA-registered enterprises are specifically granted *preferential tax treatment* by law.[40]

Thus, PEZA-registered enterprises are entitled to special privileges, such as, but not limited to, the payment of five percent (5%) of its gross income as taxes, in lieu of all national and local taxes, with the exception of real property taxes, as stated in Section 24 of R.A. No. 7916, as amended, to wit:

> **"CHAPTER III - OPERATIONS WITHIN THE ECOZONE**
>
> **SEC. 24.** *Exemption from National and Local Taxes.*- Except for real property taxes on land owned by developers, no taxes, local and national, shall be imposed on business establishments operating within the ECOZONE. In lieu thereof, five percent (5%) of the gross income earned by all business enterprises within the ECOZONE shall be paid and remitted as follows:
>
> a. Three percent (3%) to the National Government;
>
> b. Two percent (2%) which shall be directly remitted by the business establishments to the treasurer's office of the municipality or city where the enterprise is located."

[40] Section 4 (d), R.A. No. 7916, as amended by R.A. No. 8748.

As an "Ecozone Developer/Operator"[41] and "Ecozone Facilities Enterprise,"[42] respondent PIATCO is entitled to the foregoing tax exemption, as well as the other incentives specified in Rules XIV (Ecozone Developers/Operators) and Rule XVI (Ecozone Facilities Enterprise) of the *Rules and Regulations to Implement Republic Act No. 7916,* to wit:

> **"Rule XIV - Incentives to Ecozone Developers / Operators**
>
> **SECTION 1. *ECOZONE Developers / Operators*** - ECOZONE Developers / Operators shall be entitled to the following incentives:
>
> A. Exemption from National and Local Taxes and Licenses - An ECOZONE Developer / Operator shall, to the extend of its construction and operation, be **exempt from payment of all national internal revenue taxes and all local government impost, fees, licenses or taxes, including but not limited to the following**:
>
> 1. Internal revenue taxes such as gross receipts tax, **Value Added Tax**, ad valorem and excise taxes; and
>
> 2. Franchise, common carrier or value added taxes and other percentage taxes on public and service utilities and enterprises.
>
> In lieu thereof, the ECOZONE Developer / Operator Enterprise shall pay a five percent (5%) final tax on gross income in accordance with the provisions of Rule XX of these Rules.
>
> B. Additional Deduction for Training Expenses - One-half (1/2) of the value of training expenses incurred in developing skilled or unskilled labor or for managerial or other management development programs incurred by an ECOZONE Developer / Operator may be deducted from the 5% final tax due from the ECOZONE Developer / Operator but not to exceed the national governments share of three percent (3%) as provided in Section 24 of the Act, under such guidelines as may be prescribed by

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[41] Exhibit "P-26," Division Docket (CTA Case No. 9123), Vol. 5, pp. 2039 to 2049.
[42] Exhibit "P-27," Division Docket (CTA Case No. 9123), Vol. 5, pp. 2050 to 2057.

PEZA in coordination with the Department of Labor and Employment and the Department of Finance.

C. Incentives under the BOT Law - Incentives provided under R.A. 6957 as amended by R.A. 7718, otherwise known as the Build-Operate-and Transfer Law, subject to such conditions as may be prescribed by the Board.

D. Other Incentives Under the Code - Other incentives available under the Code, as may be determined by the Board subject to the conditions provided under Sections 3 and 5 of Rule XII of these Rules.

Rule XVI - Incentives to Ecozone Domestic Market, Facilities, Utilities and Tourism Enterprises

xxx xxx xxx

SECTION 2. ***ECOZONE Facilities, Utilities and Tourism Enterprises*** - ECOZONE Facilities, Utilities and Tourism Enterprises shall be entitled to the following incentives:

a. Exemption from national and local taxes and in lieu thereof payment of a special tax rate of five percent (5%) on gross income in accordance with Section 1(A) of Rule XIV and Rule XX of these Rules;

b. Additional Deduction for Training Expenses - The same incentives as provided for under Section 1(B) of Rule XIV of these Rules shall also apply to ECOZONE Facilities, Utilities and Tourism Enterprises;

c. Incentives provided under R.A. 6957 as amended by R.A. 7718, otherwise known as the Build Operate and Transfer Law, subject to such conditions as may be prescribed by the Board; and

d. Other incentives available under the Code, as may be determined by the Board subject to the conditions provided under Sections 3 and 5 of Rule XIII of these Rules." *(Emphasis supplied.)*

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In fact, petitioner himself recognizes the foregoing exemption, as stated in Revenue Regulations No. 01-00,[43] which states, in no uncertain terms, that registered ecozone enterprises, shall be exempt from *all other taxes, national or local,* except the real property tax on land owned by developers, to wit:

> "**SECTION 4.** ***Nature of the 5% Tax and Extent of Tax Exemption.*** — The above 5% tax is imposed on "gross income earned" hence, income tax in nature and a national internal revenue law in character. Registered ECOZONE enterprises shall be exempt from all other taxes, national or local, except the real property tax on land owned by developers, pursuant to Section 24 of R.A. No. 7916, as amended by R.A. No. 8748."

The subject special tax rate of five percent (5%) on gross income, in lieu of all taxes, is likewise reiterated in its respective Certificates of Registration as an Ecozone Developer/Operator and an Ecozone Facilities Enterprise, to wit:

> <u>Registration Agreement for Certificate of Registration No. EZ-98-01 as an Ecozone Developer/Operator</u>[44]
>
> "Article XIII – Special Conditions
>
> xxx xxx xxx
>
> 13.1. To the extent of the area that it shall develop, the REGISTRANT shall be entitled to the following incentives upon registration with the PEZA:
>
> a. Five percent (5%) Gross Income Tax Incentive (R.A. No. 7916);
>
> xxx xxx xxx
>
> The exemption from all national and local taxes (and payment of the 5% special tax rate on gross income), and the additional deduction for training expenses shall only be availed of upon expiration of the

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[43] Regulations Implementing Section 4 of R.A. No. 8748, Entitled, "An Act Amending Republic Act No. 7916," Otherwise Known as the Special Economic Zone Act of 1995, Amending for this Purpose Revenue Regulations No. 12-97.
[44] Exhibit "P-26," Division Docket (CTA Case No. 9123), Vol. 5, pp. 2039 to 2049.

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> Income Tax Holiday incentives, unless the REGISTRANT opts to waive all E.O. No. 226 incentives upon registration. Should the REGISTRANT opt to avail of E.O. No. 226 incentives as indicated upon registration, it shall not avail simultaneously of the incentives on exemption from all national and local taxes (and payment of the 5% gross income tax) and additional deduction for training expenses."
>
> Registration Agreement for Certificate of Registration No. 98-01-F[45] as an Ecozone Facilities Enterprise
>
> Article XI – Special Conditions
>
> "11.1. The REGISTRANT shall be entitled to the following incentives:
>
> xxx xxx xxx
>
> b. Exemption from national and local taxes and in lieu thereof, payment of a special tax rate of five percent (5%) on gross income;
>
> xxx xxx xxx
>
> The exemption from national and local taxes (and payment of the 5% special tax rate on gross income), and the additional deduction for training expenses shall only be availed of upon expiration of the ITH incentives, unless REGISTRANT opts to waive all E.O. 226/ BOT incentives upon registration. Should REGISTRANT opt to avail of E.O. 226 / BOT incentives as indicated upon registration, it shall not avail simultaneously of the incentives on exemption from all national and local taxes (and payment of the 5% gross income tax) and additional deduction for training expenses." *(Emphasis supplied.)*

From the foregoing, it is clear that the law (R.A. No. 7916, as amended), the Implementing Rules and Regulations, as well as the Registration Agreements, state, in no ambiguous terms, that respondent PIATCO, as a PEZA-registered entity, is accorded a special tax rate of five percent (5%) on gross income, in lieu of all taxes. Aside from stating that the registrant must first waive its E.O. 226 and/or BOT incentives, there is no other qualification or condition placed upon the taxpayer to enjoy such preferential rate.

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[45] Exhibit "P-27," Division Docket (CTA Case No. 9123), Vol. 5, pp. 2050 to 2057.

In this case, respondent presented its Letter[46] dated June 17, 1998, addressed to PEZA, indicating its intent to avail of the subject preferential rate. For easy reference, the pertinent portions of the subject letter are quoted herein, to wit:

> "In connection with Resolution No. 98-087 of the Board of the Philippine Economic Zone Authority (PEZA), approving the application of PIATCO for registration as an Ecozone Facilities Enterprise, we wish to inform you that PIATCO is availing of the following tax incentives:
>
> a. an exemption from all national and local taxes, and in lieu thereof, payment of a special tax rate of five percent (5%) of the gross income earned in accordance with Section 1(A) of Rule XIV and Rule XX of the Rules and Regulations to Implement Republic Act No. 7916;
>
> xxx xxx xxx
>
> We are hereby waiving the income tax holiday incentives granted under Executive Order No. 226."

With the execution of the foregoing waiver of the Income Tax Holiday Incentives granted under E.O. No. 226, respondent PIATCO is *ipso facto* entitled to the special preferential tax rate of five percent (5%) of gross income, in lieu of all other national or local taxes, including VAT.

As held in the case of *Commissioner of Internal Revenue vs. Sekisui Jushi Philippines, Inc.,*[47] a PEZA-registered entity that opts for the five percent (5%) preferential tax rate on its gross income, is exempt from *all* taxes, *including VAT*, to wit:

> "Section 23 of Republic Act 7916, as amended, gives a PEZA-registered enterprise the option to choose between two fiscal incentives: a) a five percent preferential tax rate on its gross income under the said law; or b) an income tax holiday provided under Executive Order No. 226 or the Omnibus Investment Code of 1987, as amended. If the entity avails itself of the five percent preferential tax rate under the first scheme, it is exempt from all taxes, including the VAT; under the second, it is

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[46] Exhibit " P-28," Division Docket (CTA Case No. 9123), Vol. 5, pp. 2058 to 2059.
[47] G.R. 149671, July 21, 2006.

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exempt from income taxes for a number of years, but not from other national internal revenue taxes like the VAT."

The basis for the resulting VAT exemption, which stems from availing of the five percent (5%) preferential tax rate, is further elucidated upon by the Supreme Court in the case of *Commissioner of Internal Revenue vs. Seagate Technology (Philippines),*[48] to wit:

> "Applying the special laws we have earlier discussed, respondent as an entity is exempt from internal revenue laws and regulations.
>
> xxx xxx xxx
>
> Moreover, the exemption is both express and pervasive for the following reasons:
>
> First, RA 7916 states that 'no taxes, local and national, shall be imposed on business establishments operating within the ecozone.' Since this law does not exclude the VAT from the prohibition, it is deemed included. *Exceptio firmat regulam in casibus non exceptis.* An exception confirms the rule in cases not excepted; that is, a thing not being excepted must be regarded as coming within the purview of the general rule.
>
> xxx xxx xxx
>
> Second, when RA 8748 was enacted to amend RA 7916, the same prohibition applied, except for real property taxes that presently are imposed on land owned by developers. This similar and repeated prohibition is an unambiguous ratification of the law's intent in not imposing local or national taxes on business enterprises within the ecozone."

In this case, however, petitioner contends that the tax incentive is not absolute, as it is subject to the rules and regulations of PEZA, as well as the conditions in the Registration Agreement.

This Court is not swayed.

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[48] G.R. No. 153866, February 11, 2005.

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As earlier stated, aside from requiring the waiver of the benefits under E.O. No. 226 and/or BOT incentives, there is no other condition imposed upon a PEZA-registered entity, in order to enjoy the subject preferential tax rate of five percent (5%) on gross income, in lieu of all other national or local taxes.

The provisions of law, the IRR, and even the Registration Agreements are categorical, in that PIATCO, as a PEZA-registered entity, is automatically entitled to the subject preferential tax rate, upon election thereof and waiver of the benefits of E.O. No. 226 and BOT incentives. There is no condition imposed on the PEZA-registered entities that prior approval from the PEZA is first required to avail of the said tax rate.

Assuming *arguendo,* that PEZA-registered entities are required to obtain the approval of PEZA prior to its availment of incentives under the law, this Court still finds the imposition of VAT on respondent PIATCO as erroneous.

As discussed above, PIATCO, as a PEZA-registered entity, is a VAT-exempt entity. Moreover, the importations made by PIATCO into the ecozones are considered importations into foreign territory, and are not subject to VAT. And finally, PIATCO is entitled to a special preferential tax rate of five percent (5%), and is exempted from all other national and local taxes, with the exception of real property tax.

At this juncture, this Court stresses that no less than the Supreme Court has ruled that since the establishment and operation of ecozones are of vital national importance, "in case of doubt, conflicts with respect to such tax exemption privilege shall be resolved in favor of the ecozone."[49]

From the foregoing, it is clear that the BIR has no basis for issuing the subject deficiency VAT assessments, as respondent PIATCO is a VAT-exempt entity, and its importations into the ecozones are not subject to VAT. In addition, the law grants preferential tax treatment to PIATCO as a PEZA-registered entity, thereby exempting it from all internal revenue taxes, including VAT.

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[49] *Commissioner of Internal Revenue vs. Seagate Technology (Philippines), supra.*

Considering that the subject deficiency VAT assessments are void, it can bear no fruit.[50] Thus, it becomes unnecessary to discuss the other incidental issues raised by the Petition for Review with regard to the subject assessments.

WHEREFORE, in light of the foregoing considerations, the instant *Petition for Review* is hereby **DENIED** for lack of merit. The Decision dated May 7, 2018 and the Resolution dated July 27, 2018 rendered by the Third Division of this Court, respectively, in CTA Case No. 9123 are hereby **AFFIRMED**.

SO ORDERED.

ERLINDA P. UY
Associate Justice

WE CONCUR:

ROMAN G. DEL ROSARIO
Presiding Justice

JUANITO C. CASTAÑEDA, JR.
Associate Justice

(Inhibited)
ESPERANZA R. FABON-VICTORINO
Associate Justice

CIELITO N. MINDARO-GRULLA
Associate Justice

MA. BELEN M. RINGPIS-LIBAN
Associate Justice

CATHERINE T. MANAHAN
Associate Justice

JEAN MARIE A. BACORRO-VILLENA
Associate Justice

MARIA ROWENA MODESTO-SAN PEDRO
Associate Justice

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[50] *Commissioner of Internal Revenue vs. Metro Star Superama, Inc.*, G.R. No. 185371, December 8, 2010.

CERTIFICATION

Pursuant to Article VIII, Section 13 of the Constitution, 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.

ROMAN G. DEL ROSARIO
Presiding Justice