REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

CONTEX CORPORATION,
Petitioner,

- versus -

C.T.A. CASE NO. 5895

THE HONORABLE COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:
OCT 13 2000

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DECISION

Petitioner, by way of this Petition for Review, is seeking for the refund or issuance of a tax credit certificate in the amount of P1,011,467.04, representing erroneously paid input value-added tax (VAT, for brevity) on purchases of supplies and materials for the period January 1, 1997 to December 31, 1998.

Petitioner is a domestic corporation duly organized and existing under the laws of the Republic of the Philippines, with office address located at #7 Argonaut Hi-way cor. Efficiency St., Subic Bay Industrial Port, SBMA, while its plant is located at the Subic Bay Industrial Port (SBIP) in Zambales. It is engaged in the business of manufacturing hospital textiles and garments, and other hospital supplies. It is registered with the Subic Bay Metropolitan Authority (SBMA) as a Subic Bay Freeport Enterprise pursuant to the provisions of Republic Act No. 7227, otherwise known as "The Bases Conversion Act". Being an SBMA-registered manufacturing firm, Petitioner is exempt from all local and national internal revenue taxes except for the 5% preferential tax (Exhs. D and E). It is registered with the Bureau of Internal Revenue as a non-VAT taxpayer with Certificate of Registration RDO Control No. 95-180-000133 (Exh. F).

For the period January 1, 1997 to December 31, 1998, Petitioner alleges that it purchased supplies and materials necessary in the conduct of its manufacturing business. The suppliers of these goods shifted unto Petitioner the 10% input VAT on their items. In 1997 and 1998, Petitioner alleges that it paid input taxes in the amounts of P539,411.88 and P504,057.49, respectively. Petitioner further asserts that all of its manufactured products were exported.

Petitioner, believing that it is exempt from all national and local taxes by virtue of RA 7227, including the value-added tax, filed two synonymous applications for tax credit/refund of value-added tax paid. The first letter of application, dated December 29, 1998, was filed with the office of Revenue District Officer, Mr. Edilberto Carlos of BIR Revenue District Office No. 19. Unfortunately, the application was denied. On May 4, 1999, Petitioner reiterated its application (this time) with the Regional Director, Atty. Alberto Pagabao, of BIR Revenue Region No. 4. This second letter seeks the refund or issuance of a tax credit certificate in the lesser amount of P1,108,307.72, representing erroneously paid input VAT for the period January 1, 1997 to November 30, 1998 (Annex D, CTA records, p. 13 to 17). The Regional Director did not respond to this second letter which prompted the Petitioner to file an appeal with this Court on June 29, 1999, in order to preserve its right to judicially claim the refund or credit of erroneously paid input VAT. Petitioner cites as legal bases Section 112(A) in relation with Section 106(A)(2)(a) of the Tax Code, as amended and Section 12(b) and (c) of Republic Act No. 7227.

In his Answer, Respondent raised the following special and affirmative defenses:

> 4. Petitioner's alleged claim for refund is subject to administrative routinary investigation/examination by the respondent's Bureau;
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> 5. In a claim for refund, the burden of proof is on the taxpayer to establish its right to refund, and failure to sustain the burden is fatal to the claim for refund;
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> 6. Rudimentary is the rule that claims for refund is (*sic*) construed in *strictissimi juris* against the taxpayer for they partake the nature of exemption from tax; and
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> 7. Moreover, petitioner must prove that it has complied with the governing rules with reference to tax refund, which are found in Sections 204 and 229 of the Tax Code, as amended.

The issues to be resolved by this Court are as follows:

1. Whether or not Petitioner is entitled to the claim for refund or tax credit of input VAT on supplies and materials pursuant to Section 112(A) of the Tax Code as amended; or in the alternative

2. Whether or not Petitioner is exempt from the payment of value-added tax on its purchases of supplies and materials pursuant to the proviso of Sec. 12(b) and (c) of RA 7227; and

3. Whether or not Petitioner was able to support with substantial evidence its entitlement to the claim for refund or tax credit.

In its Petition for Review, Petitioner averred that its sales were exported and subject to VAT at zero percent pursuant to Section106(A)(2)(a) of the Tax Code, as amended, to quote:

> SEC. 106. Value-Added Tax on Sale of Goods or Properties. - xxx
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> (A) Rate and Base of Tax. – There shall be levied, as assessed and collected on every sale, barter or exchange of goods or properties, value-added tax equivalent to ten percent (10%) of

the gross selling price or gross value in money of the goods or properties sold, bartered or exchanged, such tax to be paid by the seller or transferor.

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(2) The following sales by VAT-registered persons shall be subject to zero percent (0%) rate:

(a) *Export Sales.* – The term "export sales" means:

(1) The sale and actual shipment of goods from the Philippines to a foreign country, irrespective of any shipping arrangement that may be agreed upon which may influence or determine the transfer of ownership of the goods so exported and paid for in acceptable foreign currency or its equivalent in goods or services, and accounted for in accordance with the rules and regulations of the Bangko Sentral ng Pilipinas (BSP);

(2) Sales of raw materials or packaging materials to a nonresident buyer for delivery to a resident local export-oriented enterprise to be used in manufacturing, processing, packing or repacking in the Philippines of the said buyer's goods and paid for in acceptable foreign currency and accounted for in accordance with the rules and regulations of the Bangko Sentral ng Pilipinas (BSP);

(3) Sale of raw materials or packaging materials to export-oriented enterprise whose export sales exceed seventy percent (70%) of the total annual production;

(4) Sale of gold to the Bangko Sentral ng Pilipinas (BSP); and

(5) Those considered export sales under Executive Order No. 226, otherwise known as the Omnibus Investments Code of 1987 and other special laws.

Petitioner then correlates the aforequoted Section 106(A)(2)(a) with Section 112 also of the Tax Code to show its entitlement to the refund, thus:

SEC. 112. *Refunds or Tax Credits of Input Tax.* – <u>Any VAT-registered person, whose sales are zero-rated or effectively zero-rated</u> 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: *Provided, however,* That in the case of zero-rated sales under Section 106(A)(2)(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 sales 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. (Underlining supplied).

The afore-cited provisions of law do not serve as a valid basis for the claim for refund. The above provisos pertain to entities whose sales are zero-rated and are registered with the Bureau of Internal Revenue as a VAT taxpayer. On the contrary, Petitioner's sales are exempt from VAT pursuant to RA 7227 and is a non VAT taxpayer as evidenced by the Certificate of Registration RDO Control No. 95-180-000133 issued by Revenue District Officer, Rosemarie Ramos Ragasa, of BIR RDO No. 18 of the Subic Bay Freeport Zone (Exh. F). Thus, Sec. 112(A) of the Tax Code, as amended, is not a valid basis to be relied upon by Petitioner in seeking for the refund or credit of input taxes paid.

Alternatively, Petitioner relied on the provisions of Sec. 12(b) and (c) of RA No. 7227 in claiming for the refund/credit of input VAT paid, to wit:

> SEC. 12. *Subic Special Economic Zones*. -. xxx
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> (b) The Subic Special Economic Zone shall be operated and managed as a separate customs territory ensuring free flow or movement of goods and capital within, into and exported out of the Subic Special Economic Zone, as well as provide incentives such as tax and duty free **importations** of raw materials, capital and equipment. However, exportation or removal of goods from the territory of the Subic Special Economic Zone to the other part parts of the Philippine territory shall be subject to customs duties and taxes under the Customs and Tariff Code and other relevant tax laws of the Philippines.

(c) The provision of existing laws, rules and regulations to the contrary notwithstanding, no taxes, local and national, shall be imposed within the Subic Special Economic Zone. In lieu of paying taxes, three percent (3%) of the gross income earned by all businesses and enterprises within the Subic Special Economic Zone shall be remitted to the National Government, one percent (1%) each to the local government units affected by the declaration of the zone in proportion to their population area, and other factors. In addition, there is hereby established a development fund of one percent (1%) of the gross income earned by all businesses and enterprises within the Subic Special Economic Zone to be utilized for the development of municipalities outside the City of Olongapo and the Municipality of Subic, and other municipalities contiguous to the base areas.

In case of conflict between national and local laws with respect to tax exemption privileges in the Subic Special Economic Zone, the same shall be resolved in favor of the latter; (Underlining supplied).

Petitioner avers that the imposition of input VAT on its purchases of supplies and materials is erroneous because under Sec. 12(b) of RA 7227, the Subic Special Economic Zone enjoys the incentive in the form of tax and duty-free importations of raw materials. Furthermore, under Sec. 12(c) of RA 7227, no taxes, local and national shall be imposed within the Subic Special Economic Zone. Petitioner as a duly registered SBF enterprise operating within the Subic Bay Freeport Zone is entitled to the tax and duty-free incentive on its purchases of goods and is only subject to the 5% preferential tax.

We agree with the Petitioner.

Sec. 43(a) and (b) of the Rules and Regulations Implementing the Provisions Relative to the Subic Special Economic and Freeport Zone and the Subic Bay Metropolitan Authority Under Republic Act No. 7227, Otherwise Known as the "Bases Conversion And Development Act of 1992 (Rule, for brevity), provides:

SEC. 43. Tax Exemption. – SBF Enterprises shall be **exempt** from all national and local taxes, including but not limited to the following:

a. Customs and import duties and national internal revenue taxes, such as VAT, excise and ad valorem taxes on **foreign articles**;

b. Internal revenue taxes, such as VAT, ad valorem and excise taxes on their sales of goods and services for which they are directly liable;

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In lieu of paying taxes, all SBF Enterprises shall pay a final tax of five 5% percent of gross income earned in accordance to breakdown specified and defined under Section 57 hereunder.

It is clear from the above implementing Rule that an SBF enterprise shall be exempt from customs and import duties and national internal revenue taxes, such as VAT, excise and ad valorem taxes on foreign articles.

Foreign article is defined under Section 3(m) of the same Rule in this wise:

(A)rticles of foreign origin on which duties and taxes have not been paid, or upon which drawback or bounty has been allowed, or which have not been previously entered into customs territory; or articles which are the growth, product or manufacture of the Philippines on which not all national internal revenue taxes have been paid, if subject thereto, or upon which drawback or bounty has been allowed. (Underlining supplied).

It is understood that all articles administered by an SBF enterprise from Customs Territory is considered exported pursuant to Sec. 48 of the Rule, thus:

SECTION 48. *Article Administered into the SBF from Customs Territory.* – Articles which are admitted to the SBF from the Customs Territory under proper permit shall be considered exported for purposes of the laws and regulations of the Philippines, and shall be considered to be zero-rated and thereby become **eligible for drawback, relief from duties and taxes, and any other tax or duty benefit conferred by reason of exportation; *provided,* that** articles which are returned to the Customs Territory from the SBF shall be considered imported for the purposes of the laws and regulations of the Philippines. (Underscoring supplied)

We, therefore, reach a conclusion that Petitioner is exempted from the payment of input VAT on its purchases of supplies and materials. However, only the supplies and materials used by Petitioner as raw materials in manufacturing hospital textile and garments, and hospital supplies are exempt from the input VAT pursuant to the afore-quoted Section 12(b) of RA 7227. This was elucidated in Sec. 4 of Revenue Regulations No. 1-95 issued by the Department of Finance, to wit:

> SECTION 4. *Exemptions and Incentives.* –
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> A. All SBMA registered enterprises doing business within the Secured Area in the Zone shall enjoy the following:
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> a. Exemption from customs and import duties and national internal revenue taxes on importations of raw materials for manufacture into finished products and capital goods and equipment needed for their business operation within the Secured Area. Consumption items, however, must be consumed within the Secured Area. Removal of raw materials, capital goods, equipment and consumer items out of the Secured Area for sale to non-SBMA registered enterprises shall be subject to the usual taxes and duties, except as may be provided herein (underlining supplied);

Moreover, only the raw materials used by Petitioner in the manufacture of its product and which are not taken from Petitioner's premises in Subic Bay Freeport Zone are exempt from the input VAT.

Furthermore Sec. 229 of the Tax Code, as amended, provides that the recovery of erroneously paid national internal revenue tax must be instituted within two years from the date of payment of the tax.

> SEC. 229. *Recovery of Tax Erroneously or Illegally Collected.* – No suit or proceeding in any court for the recovery of any national internal revenue tax hereafter alleged to have been erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority, or of any sum alleged to have been excessively or in any manner

> wrongfully collected, until a claim for refund or credit has been duly filed with the Commissioner; but such suit or proceeding may be maintained, whether or not such tax, penalty, or sum has been paid under protest or duress.
>
> In any case, no such suit or proceeding shall be filed after the expiration of two (2) years from the date of payment of the tax or penalty regardless of any supervening cause that may arise after payment: *Provided, however*, That the Commissioner may, even without a written claim therefor, refund or credit any tax, where on the face of the return upon which payment was made, such payment appears clearly to have been erroneously paid. (Underlining supplied).

It is to be noted that the present judicial action was instituted by Petitioner on June 29, 1999, for the recovery of erroneously paid input VAT for the period January 1, 1997 to December 31, 1998. Clearly, Petitioner cannot claim the refund of input VAT paid prior to June 29, 1997 in reference to the date of filing of this Petition which was on June 29, 1999, because the same fell outside the two year period prescribed by Section 229 of the Tax Code.

In sum, the Court deemed it proper to disallow input VAT claimed by Petitioner which are already barred by prescription; or those which were imposed for maintenance, xerox, office supplies, and freight charges which cannot be categorized as raw materials; and those supplies and materials which were delivered to Makati and Pasay offices as reflected in the pre-marked invoices and official receipts.

Below is a table showing a recomputation of allowable refund due to Petitioner:

1997

SUPPLIERS	InputTaxes Claimed	DISALLOWANCES				Allowable
		Prescribed	Not a Raw Material	Invalid Inv./O.R.	Delivered in Makati/ Pasay	
3 J's Hardware	1,329.59		1,329.59			-
AP Oriental	66,482.43	29,338.52				37,143.91
Benny Manufacturing	21,347.96					21,347.96
Eagle Express Lines Inc.	894.69		894.69			-

Ever Ample Textile	37,415.18					37,415.18
Excel Colour System	23,052.52					23,052.52
Fred Rewinding Shop	1,195.45			1,195.45		
Ful Yen Enterprise	14,190.18	10,038.92				4,151.26
Garbes Dizon	1,009.09		1,009.09			-
Gems Commercial	2,229.00					2,229.00
Golden Alley Trading	2,045.45	2,045.45				-
golden Trade Ent.	502.50		502.50			-
Hency Forwarders	5,765.95		5,765.95			-
Kmbells Pack Inc.	681.82	681.82				-
Madrigal Wan Hai Lines	23,301.05		23,301.05			-
Majestic Plastic	40,855.15	16,230.90			2,072.58	22,551.67
Makati Microshop	65.45	65.45				-
New Modern Tech	2,894.55	2,894.55				-
Olongapo Lumber	226.91		226.91			-
Papyrus Educ. Supply	2,942.41		2,942.41			-
Phil. Fuji Xerox Corp.	262.21		262.21			-
Philcopy Corp.	665.45	665.45				-
Power Sustem Inc.	125.09	125.09				-
Regus Packing	15,262.51	15,262.51				-
Scanwell Consolidators	2,942.42		2,942.42			-
Supreme Packaging	160,856.48	104,413.24				56,443.24
Teresa & Sons	1,686.36		1,686.36			-
Times Trading Co.	81.09				81.09	
United Asia	32,782.33				32,782.33	-
Unix Industrial	6,523.97					6,523.97
World Link Freigh	64,477.71	64,477.71				-
XCL Business Machine	3,013.64		3,013.64			-
Zambales Lumber	2,305.27		2,305.27			-
Totals	539,411.86	246,239.61	46,182.09	1,195.45	34,936.00	210,858.71

1998

SUPPLIERS	InputTaxes Claimed	DISALLOWANCES Prescribed	Not a Raw Material	Invalid Inv/O.R.	Delivered in Makati/ Pasay	Allowable
3 J's Hardware	150.73		150.73			-
AP Oriental	44,291.69					44,291.69
Benny Manufacturing	9,502.09					9,502.09
Carlise Phils.	10,873.97					10,873.97
Champion Pack Corp.	1,641.78					1,641.78
Chrisel Ats & Prints	39,293.34					39,293.34
Dynamic Plastic	3,472.76					3,472.76
Equal Manufacturing	9,091.73					9,091.73
Excel manufacturing	29,282.90					29,282.90
Gems Commercial	829.85				829.85	-
Golden Alley Trading	1,581.82				1,581.82	-
Golden Trade Ent.	463.64		463.64			-

Goldragon Thread	19,481.32					19,481.32
JAS Enterprise	3,523.64				1,405.09	2,118.55
Kimura Chavez	16,590.91					16,590.91
Leadtech System	5,243.82					5,243.82
Majestic Plastic	21,837.23					21,837.23
Monaco Mfg Corp.	4,907.61					4,907.61
New Oriental	3,862.55					3,862.55
Olongapo Press	11,594.32		11,594.32			-
Papyrus Educ Supply	3,691.64		3,691.64			-
Phil Fuji Xerox Corp	1,750.63		1,750.63			-
Reyes Pack & Allied Mat	2,983.64					2,983.64
Slimtex Industries	20,447.60					20,447.60
Supreme Packaging	145,894.20					145,894.20
United Asia	22,819.25				10,386.60	12,432.65
Unix Industrial	23,194.67					23,194.67
Webtex Manufacturing	45,758.18					45,758.18
Totals	504,057.51	-	17,650.96	-	14,203.36	472,203.19

WHEREFORE, in view of the foregoing, the Petition for Review is hereby PARTIALLY GRANTED. Respondent is hereby **ORDERED to REFUND or** in the alternative to **ISSUE A TAX CREDIT CERTIFICATE** in favor of Petitioner the sum of P683,061.90, representing erroneously paid input VAT.

SO ORDERED.

ERNESTO D. ACOSTA
Presiding Judge

WE CONCUR:

RAMON O. DE VEYRA
Associate Judge

AMANCIO Q. SAGA
Associate Judge

CERTIFICATION

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

ERNESTO D. ACOSTA
Presiding Judge