491 Phil. 625

FIRST DIVISION

[G.R. NO. 149073, February 16, 2005]

COMMISSIONER OF INTERNAL REVENUE, PETITIONER, VS. CEBU TOYO CORPORATION, RESPONDENT.

DECISION

QUISUMBING, J.:

In its **Decision**[1] dated July 6, 2001, the Court of Appeals, in CA-G.R. SP No. 60304, affirmed the **Resolutions** dated May 31, 2000[2] and August 2, 2000,[3] of the Court of Tax Appeals (CTA) ordering the Commissioner of Internal Revenue (CIR) to allow a partial refund or, alternatively, to issue a tax credit certificate in favor of Cebu Toyo Corporation in the sum of P2,158,714.46, representing the unutilized input value-added tax (VAT) payments.

The facts, as culled from the records, are as follows:

Respondent Cebu Toyo Corporation is a domestic corporation engaged in the manufacture of lenses and various optical components used in television sets, cameras, compact discs and other similar devices. Its principal office is located at the Mactan Export Processing Zone (MEPZ) in Lapu-Lapu City, Cebu. It is a subsidiary of Toyo Lens Corporation, a non-resident corporation organized under the laws of Japan. Respondent is a zone export enterprise registered with the Philippine Economic Zone Authority (PEZA), pursuant to the provisions of Presidential Decree No. 66.[4] It is also registered with the Bureau of Internal Revenue (BIR) as a VAT taxpayer.[5]

As an export enterprise, respondent sells 80% of its products to its mother corporation, the Japan-based Toyo Lens Corporation, pursuant to an Agreement of Offsetting. The rest are sold to various enterprises doing business in the MEPZ. Inasmuch as both sales are considered export sales subject to Value-Added Tax (VAT) at 0% rate under Section 106(A)(2)(a)[6] of the National Internal Revenue Code, as amended, respondent filed its quarterly VAT returns from April 1, 1996 to December 31, 1997 showing a total input VAT of P4,462,412.63.

On March 30, 1998, respondent filed with the Tax and Revenue Group of the One-Stop Inter-Agency Tax Credit and Duty Drawback Center of the Department of Finance, an application for tax credit/refund of VAT paid for the period April 1, 1996 to December 31, 1997 amounting to P4,439,827.21 representing excess VAT input payments.

Respondent, however, did not bother to wait for the Resolution of its claim by the CIR. Instead, on June 26, 1998, it filed a **Petition for Review** with the CTA to toll the running of the two-year prescriptive period pursuant to Section 230[7] of the Tax

Code.

Before the CTA, the respondent posits that as a VAT-registered exporter of goods, it is subject to VAT at the rate of 0% on its export sales that do not result in any output tax. Hence, the unutilized VAT input taxes on its purchases of goods and services related to such zero-rated activities are available as tax credits or refunds.

The petitioner's position is that respondent was not entitled to a refund or tax credit since: (1) it failed to show that the tax was erroneously or illegally collected; (2) the taxes paid and collected are presumed to have been made in accordance with law; and (3) claims for refund are strictly construed against the claimant as these partake of the nature of tax exemption.

Initially, the CTA denied the petition for insufficiency of evidence.[8] The tax court sustained respondent's argument that it was a VAT-registered entity. It also found that the petition was timely, as it was filed within the prescription period. The CTA also ruled that the respondent's sales to Toyo Lens Corporation and to certain establishments in the Mactan Export Processing Zone were export sales subject to VAT at 0% rate. It found that the input VAT covered by respondent's claim was not applied against any output VAT. However, the tax court decreed that the petition should nonetheless be denied because of the respondent's failure to present documentary evidence to show that there were foreign currency exchange proceeds from its export sales. The CTA also observed that respondent failed to submit the approval by *Bangko Sentral ng Pilipinas* (BSP) of its Agreement of Offsetting with Toyo Lens Corporation and the certification of constructive inward remittance.

Undaunted, respondent filed on February 21, 2000, a **Motion for Reconsideration** arguing that: (1) proof of its inward remittance was not required by law; (2) BSP and BIR regulations do not require BSP approval on its Agreement of Offsetting nor do they require certification on the amount constructively remitted; (3) it was not legally required to prove foreign currency payments on the remaining sales to MEPZ enterprises; and (4) it had complied with the substantiation requirements under Section 106(A)(2)(a) of the Tax Code. Hence, it was entitled to a refund of unutilized VAT input tax.

On May 31, 2000, the tax court partly granted the motion for reconsideration in a **Resolution**, to wit:

> WHEREFORE, finding the motion of petitioner to be meritorious, the same is hereby partially granted. Accordingly, the Court hereby MODIFIES its decision in the above-entitled case, the dispositive portion of which shall now read as follows:
>
> > WHEREFORE, finding the petition for review partially meritorious, respondent is hereby ORDERED to REFUND or, in the alternative, to ISSUE a TAX CREDIT CERTIFICATE in favor of Petitioner in the amount of P2,158,714.46 representing unutilized input tax payments.
>
> SO ORDERED.[9]

In granting partial reconsideration, the tax court found that there was no need for BSP approval of the Agreement of Offsetting since the same may be categorized as

an inter-company open account offset arrangement. Hence, the respondent need not present proof of foreign currency exchange proceeds from its sales to MEPZ enterprises pursuant to Section 106(A)(2)(a)[10] of the Tax Code. However, the CTA stressed that respondent must still prove that there was an actual offsetting of accounts to prove that constructive foreign currency exchange proceeds were inwardly remitted as required under Section 106(A)(2)(a).

The CTA found that only the amount of Y274,043,858.00 covering respondent's sales to Toyo Lens Corporation and purchases from said mother company for the period August 7, 1996 to August 26, 1997 were actually offset against respondent's related accounts receivable and accounts payable as shown by the Agreement for Offsetting dated August 30, 1997. Resort to the respondent's Accounts Receivable and Accounts Payable subsidiary ledgers corroborated the amount. The tax court also found that out of the total export sales for the period April 1, 1996 to December 31, 1997 amounting to Y700,654,606.15, respondent's sales to MEPZ enterprises amounted only to Y136,473,908.05 of said total. Thus, allocating the input taxes supported by receipts to the export sales, the CTA determined that the refund/credit amounted to only P2,158,714.46,[11] computed as follows:

Total Input Taxes Claimed by respondent		P4,439,827.21
Less: Exceptions made by SGV		
a.) 1996	P651,256.17	
b.) 1997	104,129.13	755,385.30
Validly Supported Input Taxes		P3,684,441.91
Allocation:		
Verified Zero-Rated Sales		
a.) Toyo Lens Corporation	Y274,043,858.00	
b.) MEPZ Enterprises	136,473,908.05	Y410,517,766.05
Divided by Total Zero-Rated Sales		Y700,654,606.15
Quotient		0.5859
Multiply by Allowable Input Tax		P3,684,441.91
Amount Refundable		P2,158,714.[52][12]

On June 21, 2000, petitioner Commissioner filed a **Motion for Reconsideration** arguing that respondent was not entitled to a refund because as a PEZA-registered enterprise, it was not subject to VAT pursuant to Section 24[13] of Republic Act No. 7916,[14] as amended by Rep. Act No. 8748.[15] Thus, since respondent was not subject to VAT, the Commissioner contended that the capital goods it purchased must be deemed not used in VAT taxable business and therefore it was not entitled to refund of input taxes on such capital goods pursuant to Section 4.106-1 of Revenue Regulations No. 7-95.[16]

Petitioner filed a **Motion for Reconsideration** on June 21, 2000 based on the following theories: (1) that respondent being registered with the PEZA as an ecozone enterprise is not subject to VAT pursuant to Sec. 24 of Rep. Act No. 7916; and (2) since respondent's business is not subject to VAT, the capital goods it

purchased are considered not used in a VAT taxable business and therefore is not entitled to a refund of input taxes.[17]

The respondent opposed the Commissioner's **Motion for Reconsideration** and prayed that the CTA resolution be modified so as to grant it the entire amount of tax refund or credit it was seeking.

On August 2, 2000, the Court of Tax Appeals denied the petitioner's motion for reconsideration. It held that the grounds relied upon were only raised for the first time and that Section 24 of Rep. Act No. 7916 was not applicable since respondent has availed of the income tax holiday incentive under Executive Order No. 226 or the Omnibus Investment Code of 1987 pursuant to Section 23[18] of Rep. Act No. 7916. The tax court pointed out that E.O. No. 226 granted PEZA-registered enterprises an exemption from payment of income taxes for 4 or 6 years depending on whether the registration was as a pioneer or as a non-pioneer enterprise, but subject to other national taxes including VAT.

The petitioner then filed a **Petition for Review** with the Court of Appeals (CA), docketed as CA-G.R. SP No. 60304, praying for the reversal of the CTA **Resolutions** dated May 31, 2000 and August 2, 2000, and reiterating its claim that respondent is not entitled to a refund of input taxes since it is VAT-exempt.

On July 6, 2001, the appellate court decided CA-G.R. SP No. 60304 in respondent's favor, thus:

> WHEREFORE, finding no merit in the petition, this Court DISMISSES it and AFFIRMS the **Resolutions** dated May 31, 2000 and August 2, 2000 . . . of the Court of Tax Appeals.
>
> SO ORDERED.[19]

The Court of Appeals found no reason to set aside the conclusions of the Court of Tax Appeals. The appellate court held as untenable herein petitioner's argument that respondent is not entitled to a refund because it is VAT-exempt since the evidence showed that it is a VAT-registered enterprise subject to VAT at the rate of 0%. It agreed with the ruling of the tax court that respondent had two options under Section 23 of Rep. Act No. 7916, namely: (1) to avail of an income tax holiday under E.O. No. 226 and be subject to VAT at the rate of 0%; or (2) to avail of the 5% preferential tax under P.D. No. 66 and enjoy VAT exemption. Since respondent availed of the incentives under E.O. No. 226, then the 0% VAT rate would be applicable to it and any unutilized input VAT should be refunded to respondent upon proper application with and substantiation by the BIR.

Hence, the instant petition for review now before us, with herein petitioner alleging that:

I. RESPONDENT BEING REGISTERED WITH THE PHILIPPINE ECONOMIC ZONE AUTHORITY (PEZA) AS AN ECOZONE EXPORT ENTERPRISE, ITS BUSINESS IS NOT SUBJECT TO VAT PURSUANT TO SECTION 24 OF REPUBLIC ACT NO. 7916 IN RELATION TO SECTION 103 OF THE TAX CODE, AS AMENDED BY RA NO. 7716.

II. SINCE RESPONDENT'S BUSINESS IS NOT SUBJECT TO VAT, IT IS NOT ENTITLED TO REFUND OF INPUT TAXES PURSUANT TO SECTION 4.103-1 OF REVENUE REGULATIONS NO. 7-95.[20]

In our view, the main issue for our resolution is whether the Court of Appeals erred in affirming the Court of Tax Appeals resolution granting a refund in the amount of P2,158,714.46 representing unutilized input VAT on goods and services for the period April 1, 1996 to December 31, 1997.

Both the Commissioner of Internal Revenue and the Office of the Solicitor General argue that respondent Cebu Toyo Corporation, as a PEZA-registered enterprise, is exempt from national and local taxes, including VAT, under Section 24 of Rep. Act No. 7916 and Section 109[21] of the NIRC. Thus, they contend that respondent Cebu Toyo Corporation is not entitled to any refund or credit on input taxes it previously paid as provided under Section 4.103-1[22] of Revenue Regulations No. 7-95, notwithstanding its registration as a VAT taxpayer. For petitioner claims that said registration was erroneous and did not confer upon the respondent any right to claim recognition of the input tax credit.

The respondent counters that it availed of the income tax holiday under E.O. No. 226 for four years from August 7, 1995 making it exempt from income tax but not from other taxes such as VAT. Hence, according to respondent, its export sales are not exempt from VAT, contrary to petitioner's claim, but its export sales is subject to 0% VAT. Moreover, it argues that it was able to establish through a report certified by an independent Certified Public Accountant that the input taxes it incurred from April 1, 1996 to December 31, 1997 were directly attributable to its export sales. Since it did not have any output tax against which said input taxes may be offset, it had the option to file a claim for refund/tax credit of its unutilized input taxes.

Considering the submission of the parties and the evidence on record, we find the petition bereft of merit.

Petitioner's contention that respondent is not entitled to refund for being exempt from VAT is untenable. This argument turns a blind eye to the fiscal incentives granted to PEZA-registered enterprises under Section 23 of Rep. Act No. 7916. Note that under said statute, the respondent had two options with respect to its tax burden. It could avail of an income tax holiday pursuant to provisions of E.O. No. 226, thus exempt it from income taxes for a number of years but not from other internal revenue taxes such as VAT; or it could avail of the tax exemptions on all taxes, including VAT under P.D. No. 66 and pay only the preferential tax rate of 5% under Rep. Act No. 7916. Both the Court of Appeals and the Court of Tax Appeals found that respondent availed of the income tax holiday for four (4) years starting from August 7, 1995, as clearly reflected in its 1996 and 1997 Annual Corporate Income Tax Returns, where respondent specified that it was availing of the tax relief under E.O. No. 226. Hence, respondent is not exempt from VAT and it correctly registered itself as a VAT taxpayer. In fine, it is engaged in taxable rather than exempt transactions.

Taxable transactions are those transactions which are subject to value-added tax either at the rate of ten percent (10%) or zero percent (0%). In taxable transactions, the seller shall be entitled to tax credit for the value-added tax paid on