

ATLAS FERTILIZER CORPORATION, PETITIONER, VS. COMMISSIONER OF INTERNAL REVENUE, RESPONDENT.

G.R. No. L-27813. August 15, 1975

Ponente: CASTRO, J.

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CASTRO, J.:

This is a petition for review of the decision of the Court of Tax Appeals in case 1521 finding no merit in the claim of the Atlas Fertilizer Corporation (hereinafter referred to as AFC) for refund of or tax credit for alleged overpayment of sales taxes.

Sometime in 1957 the fertilizer department of the Atlas Consolidated Mining and Development Corporation (hereinafter referred to as ACMDC) was incorporated as the Atlas Fertilizer Corporation. With the approval of the Department of Finance, ACMDC transferred to AFC its tax-exemption privileges for fertilizer manufacture, a new and necessary industry under Republic Act 901. AFC enjoyed this privilege until December 31, 1962.[1]

In the manufacture of fertilizer, AFC used a mineral ingredient known as pyrite, some of which it imported and some it purchased from ACMDC. AFC did not deduct the cost of the pyrite purchased locally in computing the 7% sales tax due on its sales under Section 186 of the National Internal Revenue Code until May 1964 when, on the advice of counsel, it started to do so.

On June 18, 1964 AFC filed the present action against the Commissioner of Internal Revenue for refund of or tax credit for over payments in sales taxes on fertilizer sales made by it from June 20, 1962 to April 1964. The alleged overpayment, based on BIR data amounts to P77,310.76.

On March 15, 1967, after due hearing, the tax court rendered its decision denying AFC's claim.

Hence, the present recourse.

The basic issue is whether the cost of the pyrite AFC purchased from ACMDC and used in the manufacture of fertilizer may be deducted for purposes of computing the sales tax imposed by Section 186 of the TAX Code. This section pertinently reads:

"Sec. 186. Percentage tax on sales of other articles. — There shall be levied, assessed and collected once only on every original sale, barter, exchange, and similar transaction either for nominal or valuable considerations, intended to transfer ownership of, or title to, the articles not enumerated in sections one hundred and eighty-four and one hundred and eighty-five a tax equivalent to seven per centum of the gross selling price or gross value in money of the articles so sold, bartered, exchanged, or transferred, such tax to be paid by the manufacturer or producer: Provided, That where the articles subject to tax under this section are manufactured out of materials likewise subject to tax under this section and section one hundred and eighty-nine, the total cost of such materials, as duly established, shall be deductible from the gross selling price or gross value in money of such manufactured articles x x x"

AFC maintains that it is entitled to deduct the cost of the pyrite it purchased from ACMDC, under the authority of

Section 186-A in relation to Section 188(c) of the Tax Code. According to AFC, Section 186-A grants to a manufacturer of an article subject to the sales tax, such as fertilizer, the right to deduct the value of tax-free product used as raw material in the manufacture of the finished item from the gross selling price of the latter, while Section 188(c) exempts the sale of minerals, like pyrite, from the sales tax. AFC argues that these two provisions of the Tax Code are applicable to its fertilizer sales because pyrite is a mineral the sale of which the Code expressly exempt from the sales tax, thereby making it a tax-free product whose value it may therefore deduct from the gross selling price of its fertilizer by virtue of Section 186-A. At all events, assuming that its pyrite purchases from ACMDC do not come within the purview of the provisions of these two sections of the Tax Code, it may still deduct the cost of its pyrite purchases from ACMDC under the authority of Section 186 (supra) of the Tax Code which provides that when an article which is subject to the payment of the sales tax under that section is used as a raw material in a manufactured article subject to tax under the same section, the total cost of such raw material is deductible from the gross selling price of the finished product for purposes of computing the sales tax on the latter.

The cited Sections 186-A and 188(c) read as follows:

"Section 186-A. Whenever a tax-free product is utilized in the manufacture or production of any article, in the determination of the value of such finished article, the value of such tax-free product shall be deducted."

"Sec. 188. Transactions and persons not subject to percentage tax. — In computing the tax imposed in sections one hundred eighty-four, one hundred eighty-five, and one hundred eighty-six, transactions in the following commodities shall be excluded:

"x x x x x x x x

"(c) Minerals and mineral products when sold, bartered, or exchanged by the lessee, concessionaire, or owner of the mineral land from which removed x x x"

The Commissioner of Internal Revenue, however, contends that the term "tax-free product" as used in Section 186-A has reference only to raw materials purchased from a tax-exempt industry established under R.A. 901. He argues that before the addition of Section 186-A to the Tax Code (by virtue of R.A. 205 on June 22, 1957) the cost of raw materials purchased from tax-exempt industries was not deductible from the gross selling price of the finished product in computing the sales tax. This discouraged purchases from those industries because manufacturers preferred to use imported raw materials the total cost of which was deductible from the gross sales of their finished products as the former had been subject to sales tax prior to release from customs custody. Moreover, the pyrite which AFC purchased from ACMDC has been subject to the mining tax imposed under either Section 242 or 243 of the Tax Code, and therefore, cannot be said to constitute a "tax-free product." Neither may Section 186 be successfully invoked because pyrite is not subject to sales tax under either Section 186 or Section 189.

As to the applicability of Section 188(c) (supra), the Commissioner states that the evidence on record fails to show that the pyrite in question was sold by ACMDC as a "lessee, concessionaire or owner of the mineral land from which [the mineral or mineral product was] removed."

We are of the considered opinion that the submission of AFC is correct.

1. We have assiduously scrutinized the pertinent Congressional records to evaluate the merit of the argument that Section 186-A was incorporated into the Tax Code to benefit exclusively new and necessary industries established under R.A. 901, and have failed to find any indication that the policy and intent of R.A. 205 are as pointed out by the Commissioner. A close analysis of R.A. 205 would show that except for a section amending the tax on

capital gains, that statute's amendatory provisions are confined to Title V of the Tax Code which governs the privilege tax on businesses and occupations and, in particular, to the provisions of the said title on fixed and percentage (sales) taxes, that is, sections 180 to 189. No mention at all of R.A. 901 is made in Section 186-A; words relating the latter to the former should be found without difficulty if the two are related.

The placement of Section 186-A in the Tax Code is quite striking. Section 186 is undeniably a general provision which ordains a uniform rate of sales tax on all articles not otherwise enumerated in other sections of the Tax Code imposing a specific rate of sales tax. It also grants producers and manufacturers the right to deduct from the gross value of their finished products the cost of raw material input subject to tax under the said section and Section 189. This policy appears to be uniformly provided for in the other sections of the Code dealing with sales taxes, namely: sections 183, 184, 185 and 189. The interposition of Section 186-A among those provisions of the Tax Code clearly indicates or in the very least compelling implies but a singular legislative purpose, which is to extend (even as it limits the applicability of) Section 186-A to raw materials the sale of which is exempt from sales tax.

In *Republic Flour Mills, Inc. vs. Commissioner of Internal Revenue*[2] we repudiated the argument that Section 186-A applies only to tax-exempt industries established under R.A. 901 as prescribed in B.I.R. Circular No. V-252 dated July 15, 1957. "Indeed," the Court said, "if the Commissioner's definition were correct, it would be logical to expect that Section 186-A of the Tax Code (ante), instead of referring to 'a tax-free product' utilized in the manufacture of other articles, would have proclaimed the deductibility of the value of 'products of a tax exempt industry x x x utilized in the manufacture or production of any article.'"

2. The Commissioner and the tax court are correct in their insistence that the exemption from the payment of the sales tax provided by Section 188(c) of the Tax Code in favor of one who sells a mineral or mineral product applies only when this commodity is sold or exchanged by the lessee, concessionaire or owner of the mineral land from which the mineral or mineral product is removed. The words used in Section 188(c) plainly and literally support this view. The evidence on record, as contended by the Commissioner and correctly sustained by the tax court, does not show that ACMDC is a lessee, concessionaire or owner of the mineral land from which the pyrite bought by the AFC was removed. For this reason, AFC is misled in invoking Section 188(c) and Section 186-A of the Tax Code. The latter section allows a manufacturer or producer, of an article subject to the sales tax the right to deduct from the gross selling price or gross value in money thereof the value of a tax-free product used in the manufacture or production of the finished article. Since AFC failed to show that it acquired the pyrite in question from ACMDC under circumstances that call for the application of the exemption under Section 188(c), the sale of the said pyrite cannot therefore be considered exempt from the sales tax, and deduction under Section 186-A of the cost of such pyrite from the gross selling price of fertilizer sold by AFC to its customers would not be appropriate.

The non-applicability of Sections 188 and 186-A to the purchases of pyrite made by AFC from ACMDC, however, makes it obvious that ACMDC's pyrite sales to AFC are subject to the sales tax under Section 186 of the Tax Code, pyrite not being one of the products or commodities mentioned in sections 184 and 185[3] of the Tax Code.

Section 186 (supra), in essence, prescribes that where an article subject to the sales tax is not among those enumerated in Sections 184 and 185 of the Tax Code (which impose higher rates of sales taxes on the sale of luxury and semi-luxury items, respectively), a tax of 7% on the gross selling price or gross value in money of the article concerned shall be collected "once only on every original sale, barter, exchange, and similar transaction" of the said article. Because of this policy of imposing the sales tax only once on the original sale, the proviso of Section 186 states correspondingly that where articles subject to tax under it "are manufactured out of materials

likewise subject to tax" under Section 186 or 189[4] of the Tax Code, then "the total cost of such materials, as duly established, shall be deductible from the gross selling price or gross value in money of such manufactured articles."

The AFC's submission that under Section 186 of the Tax Code it may deduct the cost of its local purchases of pyrite from the gross selling price of its fertilizer wherein the said pyrite was used as an ingredient, must therefore be upheld.

To repeat, the main issue in the case at bar is whether the AFC is entitled under the Tax Code to deduct the purchase cost of the pyrite it used as ingredient in its manufacture of fertilizer for the purpose of computing the sales tax it must pay on its sales of fertilizer. In expounding their respective positions on this issue, the Commissioner of Internal Revenue and the Court of Tax Appeals appear to have been confused by their obsessional preoccupation with the incidental matter of whether or not the ACMDC had paid a sales tax on the pyrite it had sold to the AFC; they failed to take due stock of the organic relationship among the pertinent sections and provisions of the Tax Code involved (already hereinbefore discussed), viz., Sections 186, 186-A and 188(c), as well as a precept quite basic in the field of sales taxes.

Under Section 188(c), if the ACMDC was the lessee, owner or concessionaire of the mineral land from which it removed the pyrite that it had sold to the AFC, then it was exempt from paying any sales tax on its sales of pyrite. Any purchase — such as the AFC — of pyrite from the ACMDC may deduct the purchase cost of such pyrite under the authority of Section 186-A which provides:

"Whenever a tax-free product is utilized in the manufacture or production of any article, in the determination of the value of such finished article, the value of such tax-free product shall be deducted."

On the other hand, if the ACMDC was not qualified for exemption from sales tax on its sales of pyrite under Section 188(c) (because it was not the lessee, owner or concessionaire of the mineral land from which it removed the pyrite), then the AFC (or any other purchaser of pyrite from the former) cannot invoke Section 186-A as the legal authority for deducting the total cost of the pyrite it purchased from the ACMDC. However, it does not thereby follow that the AFC (a purchaser of pyrite from the ACMDC) is barred from deducting the purchase cost of the pyrite from the gross selling price of the manufactured article (fertilizer) sold by it. The deduction can still be made, but under the authority of Section 186 which pertinently reads:

"x x x Provided, That where the articles subject to tax under this section are manufactured out of materials likewise subject to tax under this section and section one hundred and eighty-nine, the total cost of such materials, as duly established, shall be deductible from the gross selling price or gross value in money of such manufactured articles."

The inordinate attention paid by the Commissioner of Internal Revenue and the Court of Tax Appeals to the possibility that the ACMDC did not pay any sales tax on its sales of pyrite to the AFC becomes more clearly inapropos when it is considered that, fundamentally the sales tax is an obligation of the seller and not of the buyer.[5] The Commissioner's recourse is against the ACMDC and not against the AFC, if the former did not pay any sales tax on its sales of pyrite to the AFC, assuming that ACMDC was not exempt under Section 188(c) of the Tax Code from payment of sales tax on its sales of pyrite.

ACCORDINGLY, the decision of the Court of Tax Appeals is set aside. The Commissioner of Internal Revenue is hereby ordered to credit the Atlas Fertilizer Corporation in the amount of P77,310.76 against its current or future tax liabilities. No pronouncement as to costs.

Teehankee, Makasiar, Esguerra, Muñoz Palma, and Martin, JJ., concur.

[1] R.A. 901 which took effect on June 20, 1953 revised R.A. 35. It granted "new and necessary industries" full exemption from direct internal revenue taxes until December 31, 1958 and gradually diminishing tax exemptions from January 1, 1959 to December 31, 1962.

[2] L-25602, Feb. 18, 1970, 31 SCRA 520, 526.

[3] Section 184 covers the sale of luxury items, such as jewelry, automobiles, toilet preparations (e.g., perfumes, cosmetics, essences) etc.; Section 185 covers semi-luxury items such as household appliances, watches, clocks, fishing rods, suitcases, advertising devices, etc.

[4] Section 189 imposes a percentage tax on proprietors or operators of rope factories, sugar centrals, coconut oil mills, dessicated coconut factories and cassava mills.

[5] In this jurisdiction the settled rule is that the payment of the sales tax is an obligation alone of the seller, not the purchaser, even if in the commercial world it is a usual practice among vendors to shift all or part of the tax burden to their customers. See *Abad vs. Court of Tax Appeals*, L-20834, L-20903, October 19, 1966, 18 SCRA 374, 385; *Commissioner of Internal Revenue vs. American Rubber Co., Inc.*, L-19667, November 29, 1966, 18 SCRA 853; *Philippine Acetylene Co., Inc., vs. Commissioner of Internal Revenue*, L-19707, August 17, 1967, 20 SCRA 1056; *Gil Hermanos vs. Hord*, 10 Phil. 218.

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