

H. E. HEACOCK CO., PLAINTIFF AND APPELLANT, VS. THE INSULAR COLLECTOR OF CUSTOMS, DEFENDANT AND APPELLEE.

G.R. No. 11615. April 01, 1918

Ponente: JOHNSON, J.

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JOHNSON, J.:

This appeal presents two important questions.

First. Are movements of watches, imported from Switzerland into the United States, and there placed in cases and later imported to the Philippine Islands, subject to the payment of duty?

Second. Must the Collector of Customs pay interest on the amount of duty illegally collected, which has been paid under protest, when he is ordered by the courts to return the same?

The lower court answered each of these questions in the affirmative. From that conclusion the importer appealed.

The facts in the present case have been stipulated. (See Bill of Exceptions, pp. 3-9.) The important facts are: That the plaintiff imported into the Philippine Islands 48 bracelet watches from the United States; that the movements of all of said watches had been manufactured in Switzerland and imported into the United States; that two of the cases of said watches were like wise made in Switzerland and imported into the United States; that all of the rest of the cases, including the bracelets, were manufactured in the United States; that the movements were placed in said cases in the United States; that the watches (the cases, the movements and the bracelets) were imported into the Philippine Islands with the movements placed in said cases and with the bracelets attached.

The Collector of Customs assessed and collected duty upon said watches, including the cases, the movements and the bracelets. From that decision the plaintiff appealed to the Court of First Instance, and the case was submitted there upon a stipulation of facts. After hearing the respective parties and considering the facts, the Honorable James A. Ostrand, judge, rendered a decision confirming in part and reversing in part the order of the Collector of Customs. The lower court held that the 46 cases manufactured in the United States, as well as the 48 bracelets which had also been manufactured in the United States, should have been admitted free of duty. The court further held that the two cases and the 48 movements which had been manufactured in Switzerland and imported into the United States and then later into the Philippine Islands were subject to the payment of duty. The Collector of Customs collected 25 per cent duty on the value of the watches imported, including the cases, the movements and the bracelets.

The theory of the importer and appellant is that, inasmuch as the cases, movements and bracelets had been united in the United States, the result being a watch, it was therefore a manufactured product of the United States and should be admitted free of duty under the provisions of section 12 of the Act of Congress of 1909 (Par C. of section 4 of the Act of Congress of October 3, 1913).

The theory of the Collector of Customs is that the mere placing of the imported movements in the cases and attaching the bracelets did not constitute the resulting article a manufacture in accordance with the legal definition

of that term as there was not sufficient transformation of the component parts, and no new article resulted having a distinctive name, character and use.

The Collector of Customs, in his decision of May 7, 1915, based his conclusions upon the provisions of section 12 of the Philippine Tariff Law of 1909. The fact that that law had been repealed by paragraph C of section 4 of the Act of Congress of October 3, 1913, seems to have been overlooked. While the important provisions of said section 12 were reenacted in said paragraph C of section 4, the latter contains some amendments to the former law. The amendments, however, in no way affect the result in the present case.

Section 12 of the Tariff Law of 1909 provides:

"That all articles, except rice, the growth, product, or manufacture of the United States and its possessions to which the customs tariff in force in the United States is applied and upon which no drawback of customs duties has been allowed therein, going into the Philippine Islands shall hereafter be admitted therein free of customs duty when the same are shipped directly from the country of origin to the country of destination: Provided, That direct shipment shall include in bond through foreign territory contiguous to the United States. Said articles shall be as originally packed without having been opened or in any manner changed in condition: Provided, however, That if such articles shall become unpacked while en route by accident, wreck, or other casualty, or so damaged as to necessitate their repacking, the same shall be admitted free of duty upon satisfactory proof that the unpacking occurred through accident, or necessity, and that the merchandise involved is the identical merchandise originally shipped from the United States, or its possessions as hereinbefore provided, and that its condition has not been changed except for such damage as may have been sustained."

Paragraph C of section 4 of the Tariff Law of October 3, 1913, provides:

"That there shall be levied, collected, and paid upon all articles coming into the United States from the Philippine Islands the rates of duty which are required to be levied, collected, and paid upon like articles imported from foreign countries: Provided, That all articles, the growth or product of or manufactured in the Philippine Islands from materials the growth or product of the Philippine Islands or of the United States, or of both, or which do not contain foreign materials to the value of more than 20 per centum of their total value, upon which no drawback of customs duties has been allowed therein, coming into the United States from the Philippine Islands shall hereafter be admitted free of duty: Provided, however, That in consideration of the exemptions aforesaid, all articles, the growth, product, or manufacture of the United States, upon which no drawback of customs duties has been allowed therein, shall be admitted to the Philippine Islands from the United States free of duty: And provided further, That the free admission, herein provided, of such articles, the growth, product, or manufacture of the United States, into the Philippine Islands or of the growth, product, or manufacture, as hereinbefore defined, of the Philippine Islands into the United States, shall be conditioned upon the direct shipment thereof, under a through bill of lading, from the country of origin to the country of destination: Provided, That direct shipment shall include shipments in bond through foreign territory contiguous to the United States: Provided, however, That if such articles become unpacked while en route by accident, wreck, or other casualty, or so damaged as to necessitate their repacking, the same shall be admitted free of duty upon satisfactory proof that the unpacking occurred through accident or necessity and that the merchandise involved is the identical merchandise originally shipped from the United States or the Philippine Islands, as the case may be, and that its condition has not been changed except for such damage as may have been sustained: * * *"

There are further provisos with regard to internal revenue taxes. The final proviso of paragraph C is:

"* * * And provided further, That section thirteen of 'An Act to raise revenue for the Philippine Islands, and for other purposes,' approved August fifth, nineteen hundred and nine, is hereby repealed."

Paragraph S of section 4 is in part as follows:

"That, except as hereinafter provided, sections one to forty-two both inclusive, of an Act entitled 'An Act to provide revenue, equalize duties, and encourage the industries of the United States, and for other purposes,' approved August fifth, nineteen hundred and nine, and all Acts and parts of Acts inconsistent with the provisions of this Act, are hereby repealed. * * *"

Although, in the main, while there is no difference between the provisions of the Philippine Tariff Law of 1909 and that of 1913, yet we think that the latter law must be considered as having repealed the former. In reenacting the free trade from the United States to the Philippine Islands, Congress has placed such relation upon a new ground. Congress has declared in the Act of 1913 that the reason for allowing United States products to be admitted into the Philippine Islands is "in consideration of the right to import Philippine product into the United States free of duty."

The importer contends that the lower court erred in not deciding that the "bracelet watches" as a whole were of American manufacture, and hence exempt from duty. It argues that since the watch movements had already paid a duty of 30 per cent upon their importation into the United States, they have in effect become American products by virtue of having been placed in cases of American manufacture and should therefore be exempt from duty. It further argues that the product—the bracelet watches—should be considered as a whole, as "bracelet watches" manufactured in the United States. In support of that contention it cites the case of *Uy Chaco Sons vs. Collector of Customs* (24 Phil. Rep., 548).

Before discussing the decision of this court in the case of *Uy Chaco Sons*, it is important to note just what merchandise imported from the United States are admitted free of duty into the Philippine Islands. Paragraph C above provides, among other things, that "all articles shall be admitted into the Philippine Islands from the United States free of duty, which are (a) of the growth, (b) the product, and (c) the manufacture of the United States, upon which no drawback of customs duties has been allowed therein (in the United States)." Therefore, when it is established that the merchandise in question is the growth, or the product or the manufacture of the United States, it must be admitted free of duty when it is established that no drawback of customs duties has been allowed in the United States. Certainly, the phrase "upon which no drawback of customs duties has been allowed" cannot apply to articles which are wholly of the product or manufacture of the United States. Certainly said phrase was not intended to be applied to articles "the growth or the product of the United States," because it is difficult to imagine a case when there could be a drawback of customs duties on such articles. The only case in which said phrase "drawback of customs duties," can be applied is when the product is a manufactured product of the United States, and then only when said manufactured product is composed of some article not of the growth or product of the United States. For example, in order to manufacture a particular article it becomes necessary for the manufacturer to import into the United States some of its component parts. In such case, when the manufacturer exports said manufactured article, he is entitled to a drawback of customs duties on the imported article which constituted an element of the manufactured article. We are here using the words "manufacturer" and "manufactured" in their technical sense. In our example, of course, if the exporter of such manufactured article recovers back the customs duties which he has paid, then the completed manufactured product is not admitted free of duty into the Philippine Islands. It is only when he does not ask for a repayment of the customs duties upon such .manufactured articles that they are admitted free of duty. Of course, if the imported component parts of the manufactured article is admitted free of duty into the United States, then there can be no drawback of customs duties, because none have been paid.

The phrase "when no drawback of customs duties has been allowed" only applies to articles "of the growth, product or manufacture of the United States." That being so, the fact that there has been no "drawback" does not

make the particular article admissible into the Philippine Islands. It must be an article of the growth, product or manufacture of the United States. If those facts do not exist then the articles cannot be admitted into the Philippine Islands free of duty, even though such articles are imported directly from the United States. That being true, then the only question for solution is: Are said watches, the growth, product, or manufacture of the United States? The question is still further limited to the question whether the uniting of the cases, works and bracelets produced a manufactured article of the United States, there being no contention that they were the growth or product of the United States. If they are "manufactured articles of the United States" and no "drawback" duty has been paid, then they may be admitted free of duty. If they are not "manufactured articles of the United States," then they may not be admitted free of duty, even though no "drawback" has been allowed.

In the case of *Uy Chaco Sons*, supra, the importer claimed that white lead manufactured, in a bonded warehouse in the United States, from pig lead imported from Spain without the payment of duty was entitled to free entry into the Philippine Islands. It is admitted that the pig lead had been imported into the United States from Spain: that there was a duty upon the pig lead which had not been paid by the importer; that the pig lead was subjected to a process which resulted in the "white lead," in a bonded warehouse, and was exported from the United States to the Philippine Islands, from said bonded warehouse, without having paid the prescribed duty. The court held that the "white lead" was not exempt from the payment of duty as a "manufactured article of the United States." The effect of bringing the goods to the Philippine Islands through a bonded warehouse in the United States is the same as though the "white lead" had been brought to the Philippine Islands directly from Spain—the country from which it was originally exported to the United States. The fact that it was kept in a bonded warehouse from the time of its importation in the United States until the time it was exported to the Philippine Islands prevented it from becoming in any sense the product or manufacture of the United States. It had never become a part of the product or manufacture of the United States. Apart from the fact that it had undergone some chemical changes while it was in the bonded warehouse in the United States it is in exactly the same condition which it would have been in had it been exported directly "to the Philippine Islands from Spain. It is in no sense a manufactured article of the United States and was therefore properly subjected to the payment of duty.

In the present case it is admitted that all of the movements of the said 48 watches and two of the cases had been imported into the United States and had paid the prescribed duty. It is admitted that the 46 movements were placed in the cases in the United States and later the 48 watches, as completed by the uniting of the cases, the movements and the bracelets, were imported into the Philippine Islands. No claim is made that any work or labor had been placed upon said movements or the said two cases except to place the movements in the cases after their importation into the United States. It is further admitted that no drawback of duties had been allowed. The first question, which presents itself in this relation is whether or not the bracelet watches, made as above indicated, constituted a manufactured article of the United States and fall within the provisions of the Tariff law above quoted and are therefore admissible free of duty into the Philippine Islands. The Collector of Customs held that the bracelet watches in question were not manufactured articles of the United States and were therefore not admissible free of duty into the Philippine Islands. His conclusions were modified by the lower court. The court held that the bracelets and the cases were manufactured articles of the United States and should have been admitted free of duty, but held that the movements were not a manufacture of the United States and should therefore be subjected to the payment of duty.

With reference to the question whether the watches were a manufacture of the United States we have held in many causes that, in order to constitute "a manufacture" under the Tariff Act, there must be in effect a transformation, in some way or other, of the article or articles before it will be held to be "a manufacture." (*Castle Bros.*, *Wolf & Sons vs. McCoy*, 21 Phil. Rep., 300; *Kuenzle & Streiff vs. Collector of Customs*, 32 Phil. Rep., 510; *State vs. American Sugar Refining Co.*, 51 La. Ann., 562; *State vs. Eckendorf*, 46 La. Ann., 131; *Hartranft*

vs. Wiegmann, 121 XJ. S., 609; Tide Water Oil Co. vs. United States, 171 U. S., 210.

The application of labor to an article, either by hand or by mechanism, does not make the article necessarily a manufactured article within the meaning of that term as used in the tariff law, unless the application of such labor is carried to such an extent that the article suffers a specific transformation and is changed into a new and different article, having a distinctive name, character or use. (United States vs. Semmer, 41 Fed. Rep., 324; Baumgarten vs. Magone, 50 Fed. Rep., 69; Tide Water Oil Co. vs. United States, 171 U. S., 210.)

Courts and lexicographers have differed in their definition of what constitutes a manufacture. The courts have been obliged to formulate definitions in order to give effect to the purpose of legislative enactments, while lexicographers have been free to define said terms upon the pure etymology of the words. Courts have been obliged to define the term in order to make it applicable to particular affairs. It is the duty of the court to give the Tariff Law a strict interpretation which will give force and effect to such law. The primary purpose of the law is to produce revenue. (Castle Bros., Wolf & Sons vs. McCoy, 21 Phil. Rep., 300.)

The Attorney-General, Ramon Avanceña, in his brief says:

"It is difficult indeed to conceive of the process of reasoning which would lead one to conclude that the mere insertion of imported watch movements in American cases would convert them into American products; it would be just as reasonable to claim that imported unroasted, unground coffee could be put up in American gold cans and exported as American-grown coffee. If Swiss watch works could be imported free of duty into the Philippine Islands simply because they are in American cases what would prevent the immediate returning of the cases to America for the insertion of more works, and thus use the cases over and over again as a means of bringing dutiable foreign products into the Philippine Islands to avoid the payment of the tax? And if such a practice were to be permitted what would prevent the free importation into the Philippine Islands by American wholesale liquor dealers of imported beers, wines, etc., transferred from their original containers into American-made flasks, and the repeated return of those flasks to the United States to be refilled? According to the argument of the plaintiff in this case, apparently all that would be necessary would be to make the value of the flasks exceed the value of the contents. The very purpose of tariff laws could thus be entirely defeated."

The lower court modified the decision of the Collector of Customs and held that a portion of the money paid by the importer should be returned to the importer together with 6 per cent interest per annum from the date of the original liquidation of said duties. While the Collector of Customs did not appeal from the decision of the lower court, he now asserts that that part of the judgment of the lower court in which interest was allowed was erroneous and should be modified. Inasmuch as the Collector of Customs did not appeal, we are not called upon directly to pass upon the legality of that part of the judgment. However, due to the importance of the question suggested by the Collector of Customs, we deem it advisable to call attention to the jurisprudence on that question.

It is a clearly established rule of law that a sovereign State is not liable to pay interest unless under statute or contract. That rule is settled by decisions of the Supreme Court of the United States, in decisions of supreme courts of the various States and by the courts of England. (United States vs. Bayard, 127 U. S., 251; United States vs. State of North Carolina, 136 U. S., 211; State vs. Thompson, 36 Ohio St., 409; Carr vs. The State, Ex rel. Coetlosquet, 127 Ind., 204; In re Gosman, 17 Chancery Div., 771.)

While the sovereign State, in the absence of statute or contract, is not liable to pay interest, it has been held, however, that governmental agencies, whether individuals or boards, which have been given the power to sue and to defend suits may be compelled to pay interest upon their indebtedness even though the Government itself ultimately pays the indebtedness. Tax collectors are almost universally given the power to defend suits against them for illegal collection of taxes. It is usually provided that the person taxed may protest and appeal to the

courts to have the question of the legality of the assessment determined. It is usually provided that when the courts determine that the assessment was illegal, the Government itself will refund the money, relieving the collector of personal liability. (See sec. 989, Revised Statutes of the United States.)

In the case of *Erskine vs. Van Arsdale* (15 Wall. [U. S.], 68-75), the Supreme Court of the United States held that—

"Taxes illegally assessed and paid may always be recovered back, if the collector understands from the payer that the taxes are regarded as illegal and that suit will be instituted to compel the refunding of them. * * * Where an illegal tax has been collected, the citizen who has paid it, and has been obliged to bring suit against the collector, is, we think, entitled to interest in the event of recovery, from the time of the illegal exaction." (See also *Schell vs. Cockren*, 107 U. S., 625; *National Home vs. Parrish*, 229 U. S., 496; *White vs. Arthur*, 10 Fed. Rep., 80; *McClain vs. Pennsylvania Company*, 108 Fed. Rep., 618.)

In the case of *National Home vs. Parrish* (229 U. S., 496), the Supreme Court, discussing the question before us, said:

"It is quite true that the United States cannot be subjected to the payment of interest unless there be an authorized engagement to pay it or a statute permitting its recovery. (U. S. Ex rel. *Angarica vs. Bayard*, 127 U. S., 251; U. S. vs. *State of North Carolina*, 136 U. S., 211.) But this exemption has never as yet been applied to subordinate governmental agencies. On the contrary, in suits against collectors to recover moneys illegally exacted as taxes and paid under protest, the settled rule is that interest is recoverable without any statute to that effect, and this although the judgment is not to be paid by the collector, but directly from the treasury. (*Erskine vs. Van Arsdale*, 15 Wall., [U. S.], 68-75; *Redfield vs. Bartels*, 139 U. S., 694.)"

Section 144 of the Internal Revenue Act of 1914 authorizes the Collector of Internal Revenue, in cases like the present, to pay out of public funds in his hands "any judgment, damages, or costs" recovered in an action brought against "any revenue officer" by reason of any act done in the performance of official duties. The "damages" for the wrongful exaction or withholding of money is the payment of interest at the legal rate. (Article 1108, Civil Code.)

In view of all of the foregoing, we see no reason for modifying the judgment of the lower court. The same is, therefore, hereby affirmed, with costs. So ordered.

Carson, Araullo, Street, and Malcolm, JJ., concur.

Arellano, C. J., concurs in the result.

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