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Background

The first time the Senate evaluated bills on anti-smuggling was during the 13th Congress (2004-2007)[1]. In the Senate, several bills were filed which were first referred to the Committee on Trade and Commerce. Later on, they were transferred to the Committee on Ways and Means.

During the 14th Congress (2007-2010)[2], the consolidated draft bill was refilled. During that time, the House of Representatives passed an anti-smuggling bill, which was later incorporated into the Senate version. There was smooth sailing as far as the consolidated bill was concerned because both the Senate and the House

[1] During the 13th Congress, the Chairman of the Senate Committee on Trade and Commerce was Senator Mar Roxas, while the Chairman of the Committee on Ways and Means was Senator Ralph Recto.

[2] During the 14th Congress, the Chairmen of the Senate Committee on Ways and Means were Senator Francis Escudero and Senator Panfilo Lacson.

of Representatives almost had similar provisions, until the Revised Kyoto Convention (RKC) was ratified in the Senate on February 1, 2010.[3]

At that point in time, the Bureau of Customs (BOC) drafted an entirely new version of the bill incorporating the provisions of the RKC. When the RKC was still being evaluated in the Senate, there were strong concerns from the private sector, representing the adversely affected domestic industries. The local industries were apprehensive about some of the RKC provisions which, from their point of view were too liberal. For example, under the RKC, freeports were under the direct supervision and control by the BOC. Another objectionable RKC provision was allowing the entry of imported products in the domestic market, subject to certain conditions.

In order to adhere to the RKC, the Senate rejected particular RKC provisions deemed objectionable during that time.

The Senate of the Philippines

During the current Congress (2010-2013)[4], the Senate filed the version consolidating all the Senate bills including the bill passed by the House of Representatives during the 14th Congress. SB 2408 (authored by Sen. Recto) is considered as the mother bill on anti-smuggling in the Senate. It has the following features:

1. The comments of all the affected domestic Industries were incorporated;
2. Pertinent portions of the bill reflects RKC provisions;
3. The pre-RKC version of the House of Representatives are inserted in the bill;
4. The point of view of the government sector is considered; and
5. To a certain extent, the bill was redrafted to incorporate provisions of the RKC.

The Customs and Tariff Modernization Act (CTMA)

The House of Representatives abandoned the pre-RKC bill in favor of the Customs and Tariff Modernization Act (CTMA), passing it on third reading, and subsequently sent it to the Senate for consideration on August 18, 2012. The CTMA not only amends certain provisions of the current Customs and Tariff Code of the Philippines (CTCP), it totally adopts the provisions of the RKC. The CTMA also restructures the organizational structure of the BOC.

The tariff portion of the CTMA is also in the state of flux. The worldwide trend is to form free trade areas (FTAs). The Philippines, in order to be synchronized with the trend, formed alliances through the FTAs[5]. As a result of such membership, there are several tariff agreements in order to accommodate the different tariff rates.

Gone are the days when getting a tariff rate for a particular product meant choosing between the ASEAN[6] rate and the Most-Favoured Nation (MFN) rate. At present, the procedure is more complicated because each FTA has its own tariff schedule. One of the FTAs is the PJEPA (Philippine Japan Economic Partnership Agreement) which is under review by the parties. As a consequence, there is a possibility the tariff schedule under PJEPA would be altered.

Another legislation affecting the CTMA are the fiscal incentive bills (House Bill No. 4935, Senate Bill Nos. 2142, 2379 and 2755). Currently, there are several government agencies granting incentives, like the Board of Investments, the freeports and the PEZA (Philippine Economic Zone Authority). What affects the CTMA is not the incentive aspect of the bill, rather the government agency that would administer and control such freeports or ecozones (economic zones, usually are under PEZA control).

The overlapping authority over the affected areas, as well as the fiction of law that freeports and ecozones are outside the tax jurisdiction of the Philippines, were factors considered in rejecting some provisions of the RKC. Once overlapping jurisdiction is solved by the fiscal incentives bill, perhaps, the Philippines would adhere to the pertinent objectionable of the RKC.

It would be difficult to reconcile the opposing provisions of the Senate version of the anti-smuggling bill and the CTMA. In this regard, the Senate has the tendency to abandon its own version in favor of the

[3] The Revised Kyoto Convention was ratified by the Senate on February 1, 2010 through Senate Resolution No. 220.

[4] The Chairman of the Senate Ways and Means Committee is Senator Ralph Recto, until October 15, 2012.

[5] The Philippines formed free trade areas with countries like Korea, Australia-New Zealand, India, and Japan, among others.

[6] The oldest FTA is the ASEAN (Association of South East Asian Nations). It has a tariff preferred lower tariff schedule as compared with the rest of the world whose tariff rates are higher following the most favoured nation (MFN) rule.

CTMA.

Focus on petroleum products

On February 12, 2012, the Bureau of Internal Revenue issued Revenue Regulations No. 2-2012 aiming to curb smuggling of petroleum products in Freeport Ports (freeports) and Economic Zones (ecozones)

Ecozones and freeports are considered as separate customs territories, hence imports destined them do not pay taxes and duties. If their locators, specially for ecozones, import raw materials to produce products for export, the importers do not pay taxes and duties, unless any raw material or finished product enters the domestic market. For freeports, any product transhipment does pay taxes and duties also. Any domestic product destined to ecozones and freeports is considered as Philippine exports. Petroleum products used by international shipping or international air carriers shall be zero rated[7]. If the imports, on which taxes and duties were paid, are subsequently exported, the importer shall be entitled to a refund.

The government revenue loss estimate of the Department of Energy because of oil smuggling is P60 billion. However, the estimate of the BOC is much lower, around P9.5 billion; P7 billion of which account for excise tax and P2.5 billion for import duties.

RR 2-2012 provides for the following – *"The Value-Added and Excise taxes which are due on all petroleum products[8] that are imported and/or brought directly from abroad to the Philippines, **including Freeport and Economic zones,** shall be paid by the importer thereof to the Bureau of Customs (BOC)."* The provision has the following effect:

1. It modifies the concept of ecozones and freeports that they are outside the tax jurisdiction of the country because they are considered as separate customs territory;

2. The concept of non payment of taxes and duties of all imports subject to refund (if warranted) was already introduced during the 13th Congress. The proposal was opposed by the domestic manufacturers, because according to them it takes a long time before the government issued the necessary refund thereby increasing the manufacturers' cost. The proponent[9] explained that the system would eliminate smuggling, anyway taxes and duties were paid already. Any leakage of imported products from ecozones and freeports will not affect government revenues in terms of taxes and duties. The Senate listened to the objection of the affected private sector;

3. It reinforces the bills (Senate Bill Nos. 2405, 2298 and 2095) on the tax exemptions of international carriers currently being considered in Congress because any sale of petroleum products to international carriers shall pay VAT (zero-rated VAT);

4. The RKC does not favor the treatment of ecozones and freeports as separate customs territory;

5. It is a positive step forward towards the adoption of the system of payment of taxes and duties on all imports, but subject to refund if necessary; and

6. The slow refund on the part of government regarding the paid taxes and duties on imports may be remedied by providing a fund for the purpose in the government budget, plus the issuance of the accompanying executive orders providing for deadlines for such payments.

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7 Section 106, Value-Added tax on Sale of Goods or Properties (2)(6).

8 Revenue Regulations No. 2-2012, Definition of Terms – ***Petroleum Products*** *shall refer to products formed in the case of refining crude petroleum through distillation, cracking, solvent refining and chemical treatment coming out as primary stocks from the refinery such as, but not limited to: LPG, naphtha, gasolines, solvents, kerosenes, aviation fuels, diesel oils, waxes and petrolatums, asphalt, bitumens, coke and refinery sludges, or other such refinery petroleum fractions, which have not undergone any processor treatment as to produce separate chemically-defined compounds in a pure or commercially pure state and to which various substances may have been added to render them suitable for particular uses: Provided, That the resultant product contains not less than fifty percent (50%) by weight of such petroleum products.*

9 The proposal was made by Senator Ralph Recto during a public hearing on anti-smuggling.

ASEAN Single Window

On December 5, 2005, the Philippines signed an agreement creating a single window for the ASEAN countries. Its objectives are as follows:

1. To provide a legal framework to establish and implement the ASEAN single window;
2. To ensure the implementation of regional commitments by ASEAN to establish and implement the ASEAN single window;
3. To strengthen the coordination and partnership among ASEAN Customs Administrations and relevant line ministries and agencies, and economic operators (importers, exporters, transport operators, express industries, customs brokers, forwarders, commercial banking entities and financial institutions, insurers, and those relevant to the international supply chain) to effectively and effectively implement the ASEAN Single Window[10].

A single window is defined thus – *"A facility that allows parties involved in trade and transport to lodge standardized information and documents with a single entry point to fulfil all import, export, and transit-related regulatory requirements. If information is electronic then individual data elements should only be submitted once.[11]"*

The worldwide financial difficulties prompted ASEAN to accelerate integration is order to obtain competitive advantage in worldwide trade. In this regard, the following efforts are being envisioned within ASEAN:

- 2012 – full integration with the ASEAN Free Trade Area,
- 2015 – formation of ASEAN common market, and
- 2020 – creation of a single production base and market.

Note that the RKC is a multinational treaty aiming to facilitate international trade by making uniform customs procedures. The ASEAN efforts, on the other hand focuses on having a single procedure on customs procedure towards the formation of a common market. Both agreements, the RKC and ASEAN, have a profound effect in formulating an anti-smuggling legislation, either the CTMA or the Senate version.

Observations

Foremost consideration in evaluating an anti-smuggling bill is balancing the interest of the domestic industry as against the government's interest. For the government, its interests are the prevention of the entry of prohibited importations and the collection of government revenue in the form of tariff and taxes. As far as the domestic industry is concerned, economic viability is its rallying point.

However, the concept of "domestic industry" needs redefinition. Gone are the days when domestic product means "Made in the Philippines". The trend is to redefine "domestic products" as products "Made in ASEAN". The creation of ASEAN's common market, common manufacturing base, and market integration warrants to divert the country's attention towards wider horizons. After all, treaties signed by the Philippines form part of the Philippine domestic law.

This is the reason that even if an anti-smuggling law is not passed by Congress, Philippine international trade continues by simply adhering to the mandates of foreign trade treaties. Enacting a strictly "localized" anti-smuggling law runs counter to the country's trade treaties, which in turn deters the country's competitive-ness.

The CTMA, being faithful to the RKC is more abreast with the demands of international competition.

[10] Article 5, ASEAN Single Window Agreement.
[11] http://www.wcoomd.org/ie/wto/Single%Window%20C0ncept.pdf.

1. COMMISSIONER OF CUSTOMS, *Petitioner* vs. AGFHA INCORPORATED, *Respondent,* G.R. No. 187425, March 28, 2011, Mendoza, *J.*

Facts:

The Manila International Container Port (MICP) received a shipment of bales of textile grey cloth on December 12, 1993. However, the Commissioner of Customs (Commissioner) held on to the shipment because its consignee/owner was allegedly fictitious. Respondent AGFHA intervened, stating that it was the owner and consignee of the shipment. On September 5, 1994, following seizure and forfeiture proceedings, the District Collector of Customs rendered a decision in favor of the government. The subsequent appeal filed by AGFHA was dismissed by the Commissioner on August 25, 1995.

The Court of Tax Appeals (CTA) Second Division on November 4, 1996 reversed the above decision of the Commissioner and ordered the release of the shipment to AGFHA. An entry of judgment was issued on November 27, 1996. On May 20, 1997 AGFHA filed a motion for execution.

On June 4, 1997, the CTA Second Division issued a Resolution holding in abeyance its action on the Motion for Execution. This is in view of the Commissioner's appeal with the Court of Appeals (CA). On May 31, 1999 the latter denied due course to the Commissioner's appeal for lack of merit.

Subsequently, the Commissioner elevated the CA ruling to the Supreme Court (SC) via a petition for review on *certiorari*. The SC dismissed the petition on October 2, 2001 and later denied it with finality on January 14, 2002. On March 18, 2002, the Entry of Judgment was issued by the SC declaring the decision final and executory as of February 5, 2002. A Writ of Execution (October 16, 2002) was issued by the CTA Second Division ordering the Commissioner to effect the release of the shipment. The Writ was not satisfied, hence the CTA adjudged the Commissioner liable to AGFHA and ordered the payment of US$160,348.08.

On June 10, 2005, the Commissioner filed a Motion for Partial Reconsideration espousing that: (1) AGFHA's claim must be pursued and filed with the Commission on Audit (COA) by virtue of Presidential Decree [PD] No. 1445[1]; (2) value should be based on the acquisition cost at the time of importation; and (3) taxes and duties must be deducted.

The CTA En Banc affirmed the CTA Second Division deciding that the Bureau of Customs (BOC) is liable to AGFHA, INC. in the sum of ONE HUNDRED SIXTY THOUSAND THREE HUNDRED FORTY EIGHT AND 08/100 US DOLLARS (US$160,348.08), subject to the payment of taxes and duties. The BOC's liability may be settled in Philippine Peso, computed at the exchange rate applicable at the time of actual payment, with interest thereon at 6% per annum computed from February 1993 up to the finality of the Resolution. Instead of the 6% interest, the rate of legal interest shall be 12% p.a. upon finality of the Resolution, until the amount is paid in full. *"The payment shall be taken from the sale or sales of the goods or properties which were seized or forfeited by the Bureau of Customs in other cases."*

Issue:

Was the CTA correct in awarding AGFHA INCORPORATED the amount of US$ 160,348.08 as payment for the value of the lost shipment that was in the BOC's custody?

Held:

The SC decided in favor of AGFHA INCORPORATED, emphasizing that respondent "x x x is entitled to recover the value of its lost shipment based on the acquisition cost at the time of payment."

The Court ruled that "x x x the rate of exchange for the conversion in the peso equivalent should be the prevailing rate at the time of payment. The Court's pronouncement is hereby quoted:

> *"In ruling that the applicable conversion rate x x x is the rate at the time of payment, the Court of Appeals cited the case of Zagala v. Jimenez, interpreting the provisions of Republic Act No. 529, as amended by R.A. No. 4100. Under this law, stipulations on the satisfaction of obligations in foreign currency are void. Payments of monetary obligations, subject to certain exceptions, shall be discharged in the currency which is the legal tender in the Philippines. But since R.A. No. 529 does not provide for the rate of exchange for the payment of foreign currency obligations incurred after its enactment, the Court held in a number of cases that the rate of exchange for the conversion in the peso equivalent should be the prevailing rate at the time of payment."* [Emphasis supplied]

On the question involving state immunity from suit, the SC declared that the petitioner cannot avoid culpability. It said that the factual circumstances of the present case *"x x x warrant its exclusion from the purview of the state immunity doctrine."* The SC said:

> *"X x x, we enunciated that this Court, as the staunch guardian of the people's rights and welfare, cannot sanction an injustice so patent in its face, and allow itself to be an instrument in the perpetration thereof. Over time, courts have recognized with almost pedantic adherence that what is inconvenient and contrary to reason is not allowed in law. Justice and equity now demand that the State's cloak of invincibility against suit and liability be shredded."*

The Commissioner was ordered to pay AGFHA INCORPORATED the amount of US$160,348.08, to be computed at the rate of exchange prevailing at the time of actual payment, subject to the appurtenant customs duties and/or taxes.

Corollary to the above, the constitutional provision on state immunity from suit can be found under the General Provisions of the 1987 Philippine Constitution, Article XVI, Section 3 which states:

"*The State may not be sued without its consent*."

As explained by a prominent author[2]:

> "*The basic postulate enshrined in the constitution that the 'State may not be sued without its consent' reflects nothing less than a recognition of the sovereign character of the State and an express affirmation of the unwritten rule effectively insulating it from the jurisdiction of courts. It is based on the very essence of sovereignty. A sovereign is exempt from suit, not because of any formal conception or obsolete theory, but on the logical and practical ground that there can be no legal right against the authority that makes the law on which the right depends.*
>
> *"The principle of state immunity from suit also rests on reason of public policy – that public service would be hindered, and the public endangered if the sovereign authority could be subjected to law suits at the instance of every citizen and consequently controlled in the uses and dispositions of the means required for the proper administration of the government.*

[1] The Government Auditing Code of the Philippines .

[2] Agpalo, Ruben E.: Philippine Political Law, pp. 6-7.

"The doctrine of sovereign immunity from suit may be invoked by any foreign state when it is sued in the country, just as the Philippines may invoke sovereign immunity from suit filed in a foreign country, except when it waives it, the suit will fail," (Italics supplied)

The offended party, however, is not without a recourse. It has been said: "*By engaging in a particular business through a governmental agency or corporation, the state divests itself of its sovereign character and makes itself amenable to suit, for in the conduct of such business there can be no one law for the sovereign and another for the subject and both should stand upon equality before the law*."

"X x x.

"*However, when the State gives its consent to be sued, it does not thereby necessarily consent to an unrestrained execution against it. When the State waives its immunity, all it does is to give the other party an opportunity to prove that the State has a liability. X x x. Disbursement of public funds must be covered by the corresponding appropriation as required by law. The functions and public service rendered by the State cannot be allowed to be paralyzed or disrupted by the diversion of public funds from their legitimate and specific objects, as appropriated by law*." (Supra, pp. 12-13)

2. **COMMISSIONER OF INTERNAL REVENUE, *Petitioner* vs. PL MANAGEMENT INTERNATIONAL PHILIPPINES, INC., *Respondent*, G.R. No. 160949, April 4, 2011, Bersamin, *J*.**

Facts:

Respondent PL Management International Philippines, Inc. (PL Management) earned an income of P24,000,000.00 in 1997, due to the professional services it performed to its client. The client, as the withholding agent, withheld the amount of P1,200,000.00 representing respondent's income tax.

In respondent's 1997 income tax return (ITR) filed on 13 April 1998, it reported a net loss of P983,037.00. Respondent also signified that it had a creditable withholding tax of P1,200,000.00 for taxable year 1997 to be claimed as tax credit for taxable year 1998.

Subsequently, on 13 April 1999, PL Management submitted its ITR for taxable year 1998 and declared a net loss of P2,772,043.00; hence it was not able to avail or claim the P1,200,000.00 as tax credit.

Respondent PL Management filed on 12 April 2000 a written claim for refund of the P1,200,000.00 unutilized creditable withholding tax for taxable year 1997. The Commissioner of Internal Revenue (CIR) did not act on the claim.

In commencing its judicial action, the respondent filed a petition for review with the Court of Tax Appeals (CTA – No. 6107) on *April 14, 2000*, because of the CIR's non-action. The CTA denied PL Management's petition holding that the claim for refund has prescribed as it was filed beyond the two-year prescriptive period as required under Sections 204(C) and 229 of the National Internal Revenue Code (NIRC), as amended.

The case was appealed to the Court of Appeals (CA) by respondent. The CA decided on November 28, 2002 (G.R. Sp. No. 68461) that the "X x x two-year prescriptive period, which was not jurisdictional, might be suspended for reasons of equity[3].

The dispositive portion of the CA decision states:

"WHEREFORE, the petition is partly GRANTED and the assailed CTA Decision partly ANNULLED. Respondent Commissioner of Internal Revenue is hereby ordered to refund to petitioner PL Management International Phils., Inc., the amount of P1,200,000.00 representing its unutilized creditable withholding tax in taxable year 1997."

The Motion for Reconsideration (MR) was rejected.

Issues:

Petitioner CIR alleges that:

1. *THE COURT OF APPEALS ERRED IN HOLDING THAT THE TWO-YEAR PRESCRIPTIVE PERIOD UNDER SECTION 229 OF THE TAX CODE IS NOT JURISDICTIONAL, THUS THE CLAIM FOR REFUND OF RESPONDENT IS SUSPENDED FOR REASONS OF EQUITY."*
2. *"THE COURT OF APPEALS ERRED IN HOLDING THAT RESPONDENT'S JUDICIAL RIGHT TO CLAIM FOR REFUND BROUGHT BEFORE THE COURT OF APPEALS ON APRIL 14, 2000 WAS ONE DAY LATE ONLY."*

Held*:*

The Supreme Court (SC) held:

"We reverse and set aside the decision of the CA to the extent that it orders the

[3] The CA cited *Oral and Dental College vs. CTA and CIR vs. Philamlife Ins. Co*.

petitioner to refund to the respondent the P1,200,000.00 representing the unutilized creditable withholding tax in taxable year 1997, but permit the respondent to apply that amount as tax credit in succeeding taxable years until fully exhausted."

The SC quoted Section 76 of the Tax Code which states:

> ***"SEC. 76. Final Adjustment Return.*** *- Every corporation liable to tax under Section 27 shall file a final adjustment return covering the total taxable income for the preceding calendar or fiscal year. If the sum of the quarterly tax payments made during the said taxable year is not equal to the total tax due on the entire taxable income of that year, the corporation shall either:*
>
> *"(A) Pay the balance of tax still due; or*
> *"(B) Carry-over the excess credit; or*
> *"(C) Be credited or refunded with the excess amount paid, as the case may be.*
>
> *"In case the corporation is entitled to a tax credit or refund of the excess estimated quarterly income taxes paid, the excess amount shown on its final adjustment return may be carried over and credited against the estimated quarterly income tax liabilities for the taxable quarters of the succeeding taxable years.* ***Once the option to carry-over and apply the excess quarterly income tax against income tax due for the taxable quarters of the succeeding taxable years has been made, such option shall be considered irrevocable for that taxable period and no application for cash refund or issuance of a tax credit certificate shall be allowed therefor****."*

The SC explained that the two options may be availed of in the alternative, i.e., the choice of one precludes the other. The decision added:

> *"The first option is relatively simple. Any tax on income that is paid in excess of the amount due the government may be refunded, provided that a taxpayer properly applies for the refund.*
>
> *"The second option works by applying the refundable amount, as shown on the FAR[4] of a given year, against the estimated quarterly income tax liabilities of the succeeding taxable year."*
>
> "X x x.
>
> *"X x x. The evident intent of the legislature, in adding the last sentence to Section 76 of the NIRC of 1997, is to keep the taxpayer from flip-flopping on its options, and avoid confusion and complication as regards said taxpayer's excess tax credit. X x x.*
>
> *"X x x.*
>
> *"The Court similarly disagrees in the declaration of the Court of Appeals that to deny the claim for refund of BPI, because of the irrevocability rule, would be tantamount to unjust enrichment on the part of the government. X x x. The amount being claimed as a refund would remain in the account of the taxpayer until utilized in succeeding taxable years, as provided in Section 76 of the NIRC of 1997. X x x unlike the option for refund of excess income tax, which prescribes after two years from the filing of the FAR, there is no prescriptive period for the carrying over of the same. Therefore, the excess income tax credit of BPI, which it acquired in 1998 and opted to carry over, may be repeatedly carried over to succeeding taxable years, i.e., to 1999, 2000, 2001, and so on and so forth, until actually applied or credited to a tax liability of BPI.*
>
> *"X x x.*
>
> *"However, in view of its irrevocable choice, the respondent remained entitled to utilize that amount of P1,200,000.00 as tax credit in succeeding taxable years until fully exhausted. In this regard, prescription did not bar it from applying the amount as tax credit considering that there was no prescriptive period for the carrying over of the amount as tax credit in subsequent taxable years."*

[4] FAR: Final Adjustment Return.

Hence, PL Management is not entitled to the refund by virtue of the irrevocability rule under Section 76 of the Tax Code of 1997.

In addition to the above SC elucidation, the following comment has been forwarded:[5]

"*Originally Section 69. The provision was amended to delineate the options available with respect to the resulting tax deficiency or excess, as the case may be, as determined upon the filing of the corporation's final adjustment return. If there is a balance in the tax due, then the corporation must pay said balance. If there is excess credit, the corporation may carry over the same. The corporation may be credited or refunded if there is any excess amount paid.*

"The section now provides that if a corporation exercises the option to carry over and apply the excess tax against the tax due for the succeeding year, the option becomes irrevocable for the taxable period." (Underscoring supplied)

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[5] Dascil, Rodelio T.: NIRC of the Philippines, 3rd Revised Ed., p. 177.