November 24, 2016

BIR RULING NO. 412-16

RA No. 7916; Sections 134 & 141, NIRC

Stepan Philippines Quaternaries, Inc.
Cocochem Agro-Industrial Park
San Antonio, San Pascual, Batangas

Attention: *AAA*

Gentlemen :

This refers to your letter dated June 7, 2016 requesting, on behalf of Stepan Philippines Quaternaries, Inc. (the "Company"), for a ruling that the importation of denatured ethyl alcohol is exempt from excise tax under Section 134 of the National Internal Revenue Code of 1997 ("Tax Code") and subject to zero percent (0%) value-added tax (VAT) on account of the Company's registration with the Philippine Economic Zone Authority (PEZA) under Republic Act (RA) No. 7916, otherwise known as "The Special Economic Zone Act of 1995."

It is represented that the Company is duly registered with PEZA as an Ecozone Export Enterprise, with PEZA Certificate of Registration No. 05-20 dated April 27, 2005, with business address at Cocochem Agro-Industrial Park in San Antonio, San Pascual, Batangas; that its registered business activity is to manufacture esterquat or ingredients for fabric softener, other quaternaries and tertiary amine derivatives for export; that denatured alcohol is one of the raw materials used by the Company in producing esterquat which is the primary ingredient in producing fabric softener; that currently, the Company is sourcing the denatured ethyl alcohol from a domestic supplier but in order to make the Company's esterquat products competitive in the market, the Company shall directly import denatured ethyl alcohol from various suppliers; and that the Company's permit as buyer/user of denatured alcohol has been renewed by the BIR on February 10, 2016 valid until December 31, 2016.

In reply, please be informed that Section 141 of the Tax Code, as amended by

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Republic Act (RA) No. 10351, provides as follows:

> *"SEC. 141.* ***Distilled Spirits.*** *— On distilled spirits, subject to the provisions of Section 133 of this Code, an excise tax shall be levied, assessed and collected based on the following schedules:*
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> xxx xxx xxx
>
> *"(b) Effective on January 1, 2015*
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> *"(1) An ad valorem tax equivalent to twenty percent (20%) of the net retail price (excluding the excise tax and the value-added tax) per proof; and*
>
> *"(2) In addition to the ad valorem tax herein imposed, a specific tax of Twenty pesos (P20.00) per proof liter.*
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> *"(c) In addition to the ad valorem tax herein imposed, the specific tax rate of Twenty pesos (P20.00) imposed under this Section shall be increased by four percent (4%) every year thereafter effective on January 1, 2016, through revenue regulations issued by the Secretary of Finance.*
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> xxx xxx xxx
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> *"This tax shall be proportionally increased for any strength of the spirits taxed over proof spirits, and the tax shall attach to this substance as soon as it is in existence as such, whether it be subsequently separated as pure or impure spirits, or transformed into any other substance either in the process of original production or by any subsequent process.*
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> *"**'Spirits or distilled spirits'** is the substance known as **ethyl alcohol, ethanol** or spirits of wine, including all dilutions, purifications and mixtures thereof, from whatever source, by whatever process produced, and shall include whisky, brandy, rum, gin and vodka, and other similar products or mixtures."*
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> xxx xxx xxx (Emphasis supplied)

On the other hand, Section 134 of the NIRC provides, to wit:

> *"SECTION 134.* ***Domestic Denatured Alcohol.*** *— Domestic alcohol of not less than one hundred eighty degrees (180°) proof (ninety percent (90%) absolute alcohol) shall, when suitably denatured and rendered unfit for oral intake, be exempt from the excise tax prescribed in Section 141: Provided, however, That such denatured alcohol shall be subject to tax under Section 106 (A) of this Code: Provided, further, That if such alcohol is to be used for motive power, it shall be taxed under Section 148(d) of this Code: Provided, finally, That any alcohol, previously rendered unfit for oral intake after denaturing but subsequently rendered fit for oral intake after undergoing*

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fermentation, dilution, purification, mixture or any other similar process shall be taxed under Section 141 of this Code and such tax shall be paid by the person in possession of such reprocessed spirits."

Based on the foregoing, it is clear that distilled spirits, which is *"the substance known as ethyl alcohol, ethanol, etc.,"* is generally subject to excise tax under the afore-quoted Section 141 of the NIRC. Thus, domestic alcohol, which falls within the meaning of "distilled spirits" is also subject to excise tax under the aforesaid Section. The exception to this rule is set forth under Section 134 of the same Code when the following requisites are met, to wit: (1) when the domestic alcohol is not less than 180° proof or 90% absolute alcohol; (2) when the same is suitably denatured; and (3) when it is rendered unfit for oral intake. Please take note, however, that the exemption from excise tax under Section 134 of the NIRC pertains only to domestic alcohol that is compliant with the requisites set forth therein. In the instant case, the subject of the request for exemption from excise tax is **imported** denatured ethyl alcohol which does not fall within the purview of Section 134 of the NIRC. Hence, your request for exemption from excise tax on your importation of denatured ethyl alcohol cannot be granted for lack of legal basis. The importation of denatured ethyl alcohol is subject to excise tax under Section 141 of the NIRC.

It bears stressing that tax exemptions are construed in *strictissimi juris* against the taxpayer and liberally in favor of the taxing authority. The basic principle in the construction of laws granting tax exemptions has been very stable. He who claims an exemption from his share of the common burden of taxation must justify his claim by showing that the Legislature intended to exempt him by words too plain to be beyond doubt or mistake (*City of Iloilo, et al. vs. Smart Communications, Inc., G.R. No. 167260*, dated February 27, 2009).

Moreover, the Permit to Buy/Use Denatured Alcohol dated March 11, 2008, renewed on February 10, 2016, issued by the BIR to the Company, contains the following conditions, among others, that have to be met by the Company in buying/using denatured alcohol:

1. The denatured alcohol shall only be purchased from a duly registered distiller/dealer of denatured alcohol holding a valid Permit to Operate as Distiller/Dealer of denatured alcohol duly issued by BIR.

2. The denatured alcohol to be purchased by the Company has been suitably denatured in accordance with existing guidelines and procedures in the denaturing of ethyl alcohol and pursuant to the denaturing formula duly approved by the BIR.

The above conditions set forth in the Permit to Buy/Use Denatured Alcohol only allow the Company to use/buy denatured ethyl alcohol from local suppliers that are duly registered with the BIR. It is worthy to mention that non-compliance with or violation of any

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of the conditions for the grant of the Permit to Buy/Use Denatured Alcohol shall be a valid ground for the revocation of the same.

Anent your claim that the subject importation of denatured ethyl alcohol is subject to zero percent (0%) VAT on account of the Company's registration with PEZA under RA No. 7916, it should be noted that the PEZA Certification dated December 18, 2015 issued to the Company, provides:

> *"This is to further certify that SPQI is a qualified enterprise for the purpose of VAT zero-rating of its transactions with its* ***local suppliers of goods, properties and services*** *in connection with its PEZA-registered activities, in accordance with Sections 4.106-6 and 4.108-6 of Revenue Regulations No. 16-2005, the Consolidated Value Added Tax Regulations 2005."* (Emphasis supplied)

Relative thereto, Sections 4.106-6 and 4.108-6 of Revenue Regulations (RR) No. 16-2005 state:

> *"SECTION 4.106-6. Meaning of the Term "Effectively Zero-rated Sale of Goods and Properties." — The term "effectively zero-rated sale of goods and properties" shall refer to the* ***local sale of goods and properties by a VAT-registered person to a person or entity who was granted indirect tax exemption under special laws or international agreement.*** *Under these Regulations, transactions which, although not involving actual export, are considered as "constructive export" shall be entitled to the benefit of zero-rating, such as local sales of goods and properties to persons or entities covered under pars. (a) no. (3) — (sale to export-oriented enterprises), (a) no. (6) — (sale of goods, supplies, equipment and fuel to persons engaged in international shipping or international air transport operations), (b) (Foreign Currency Denominated Sale) and (c) (Sales to Tax-Exempt Persons or Entities) of the preceding section."*
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> XXX XXX XXX
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> *"SECTION 4.108-6. Effectively Zero-Rated Sale of Services. — The term "effectively zero-rated sales of services" shall refer to the local sale of services by a VAT-registered person to a person or entity who was granted indirect tax exemption under special laws or international agreement.* ***Under these Regulations, effectively zero-rated sale of services shall be limited to local sales to persons or entities that enjoy exemptions from indirect taxes under subparagraph (b) nos. (3), (4) and (5) of this Section."*** (Emphasis supplied)

The above provisions cited by PEZA in its Certification dated December 18, 2015 merely grant PEZA-registered entities VAT zero-rating on its **local purchases** of goods, properties and services. Hence, the Company cannot invoke said provisions in claiming VAT zero-rating or VAT exemption on its **importation** of the denatured ethyl alcohol.

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In view of the foregoing, your request that the importation of denatured ethyl alcohol be exempt from excise tax and be subject to zero percent (0%) VAT on account of the Company's registration with PEZA is hereby denied for lack of legal basis.

Please be guided accordingly.

Very truly yours,

(SGD.) CAESAR R. DULAY
Commissioner of Internal Revenue

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