



# Expanding the Philippine Oil Pipelines

Atty. EMMANUEL M. ALONZO  
Legal & Tariff Branch

The issue of expanding the Philippine oil pipeline system has caught the attention of the legislature with the filing of SBN-2863<sup>1</sup>. The bill rationalizes that oil pipelines are more advantageous vis-à-vis using barges, lorries and trucks because the former are faster, steady, efficient, safe and cost effective modes of transport; they are not affected by weather disturbances such as typhoon, flooding and other tidal changes; they help reduce traffic congestion; there is lower risk of product contamination; and they have a lower carbon footprint.

## History of pipelines<sup>2</sup>

Pipelines are generally the most economical way to transport large quantities of oil, refined oil products or natural gas over land as compared to shipping by railroad. Pipelines have lower cost per unit and higher capacity. Although pipelines may be built under the sea, it is economically and technically demanding. Hence, transport of oil and oil products are done through tanker ships.

Oil pipelines are made of steel or plastic tubes with inner diameter typically from 4 feet (0.91 to 1.8 m). The oil is kept in motion by pump stations along the pipeline, and usually flows at speeds of about 1 to 6 meters per second (3.3 to 20 ft/s). Multi-product pipelines are used to transport two or more different products in sequence in the same pipeline. Usually in multi-product pipelines, there are no physical separation between the different products. Some mixing products are added based on pre-calculated absorption rates.

<sup>1</sup> SB 2863 is sponsored by Senator Teofisto “TG” L. Guingona.

<sup>2</sup> [http://en.wikipedia.org/wiki/Pipeline\\_transport](http://en.wikipedia.org/wiki/Pipeline_transport), July 13, 2011.

Crude oil contains varying amounts of wax or paraffin, and in colder climates causes the build up of materials within the pipeline. Often these pipelines are inspected and cleaned using pipeline inspection gauges or *pigs*, also known as *scrappers* or *go-devils*. Smart pigs (also known as intelligent or intelligence pigs) are used to detect anomalies in the pipes such as dents, metal loss caused by corrosion, cracking or other mechanical damage. These devices are launched from pig-launcher stations and travel through the pipeline to be received at any station downstream, either cleaning wax deposits and material that may have accumulated inside the line or inspecting and recording the condition of the line.

For natural gas, pipelines are constructed of carbon steel and varying in size from 2 to 60 inches (51 to 1,500 mm) in diameter, depending on the type of pipeline. The gas is pressurized by compressor stations and is odourless unless mixed with a mercaptan odorant where required by a regulating authority.

### Central Luzon oil pipeline

The existing Central Luzon oil pipeline stretches from the oil refineries in Batangas to the Pandacan oil depot in Manila. It was built in the 1970's to deliver diesel, kerosene, jet fuel, gasoline, and other fuel products. It is a 117-kilometer pipeline called the white oil pipeline system (WOPL). Another pipeline is a 105-kilometer stretch from Batangas to Sucat, Parañaque, and is called the black oil pipeline system (BOPL). Both the WOPL and the BOPL are owned by the First Philippine Industrial Corporation (FPIC).

In July 2010, residents of the West Tower Condominium in Makati and the neighboring areas complained of irritating fumes emanating from the basement of the condominium. The residents complained of headaches, nausea, respiratory ailments, eye irritation and other afflictions. Due to the said complaints, the City Government of Makati ordered the West Tower Condominium evacuated. During the investigation, it was found out that fuel products as well as water, accumulated in the basement of the condominium. It was established that there was leakage from the WOPL and seeped into the basement of the condominium.

Some 9 thousand drums or 1.8 million liters of fuel leaked from the WOPL. The FPIC insisted that such amount of leakage is within the allowable level of loss<sup>3</sup>. Note that the pipeline is relatively new and there was no notable earthquake when the incident occurred. As of presstime, the FPIC and the government are jointly conducting clean up operations.



### Pandacan oil depot

The Pandacan depot sits in a 33 hectare land along the Pasig river and is surrounded by private residences, the Malacañang Palace, and the Polytechnic University of the Philippines. The Pandacan depot is used by the three major oil companies namely, Caltex, Shell and Petron. The move to relocate the depot was triggered by the September 11, 2001 terrorist attack of New York's World Trade Center. Such attack left an indelible mark in the Filipino psyche, resulting in the following issues<sup>4</sup>:

1. **Security risk** – The depot is located in a densely populated area. Being near the Malacañang Palace, it is a magnet for terrorist attacks.
2. **Highly flammable products** – Aside from petroleum, the oil depot also stores LPG and aviation fuel (avgas), considered as highly flammable and volatile products.
3. **Ecological balance** - The depot destroys the ecological balance in the area. In case of a terrorist attack, the Pasig river would further be polluted.

Oppositions to the depot's relocation posed the following counter arguments:

1. **Loss of employment** – Relocating the oil depot means the loss of employment of many people;
2. **Duration of the relocation** – The process of relocating an oil depot takes more than 5 years to complete. Also the personnel currently employed will have to wait for a long period before being reemployed;
3. **Huge expenditure** – The proposal to relocate also needs huge capital outlay for the entities concerned;

<sup>3</sup> <http://opinion.inquirer.net/7365/back-to-normal-in-bangkal>; July 11, 2011.

<sup>4</sup> <http://www.pinoyexchange.com/forums/showthread.php?t=103941>, July 11, 2011.

4. **Non pollutant** – According to Caltex Philippines, Pilipinas Shell, and Petron Corporation, their respective oil depots have been existing under strict international standards on health, safety and security;
5. **Effect on the Pasig river** – There are no processing activities in Pandacan oil depot. It is only used as a storage area, a holding facility. In this regard, it is not polluting the Pasig river;
6. **More trucks on the road** - In the meantime the new oil depot is under construction, thousands of delivery trucks would shuttle between the refineries and Manila to keep up with the demand of Metro Manila; and
7. **Temporary increase in oil prices** – In the meantime the new oil depot is being constructed, the retail prices of oil products would increase. Transporting oil through pipelines is cheaper than transporting them through barges and trucks.

Petron Corporation's plan is to relocate its depot out of the Pandacan depot in compliance with the Supreme Court decision. It may take at least 7 years and at a cost of around Php 10 billion. The estimated cost includes the possible cost of reclamation where the future depot will be constructed.

On the other hand, Shell prefers to stay in Pandacan. Shell supplies 70 percent of the fuel requirements of the Philippines. According to Shell, once Petron vacates the area, the depot would be smaller, posing lesser risk to the surrounding areas. Nevertheless, Pilipinas Shell country chairman Ed Chua says: *"Not in this point in time, but of course you always look at fall back options. Things change in time"*<sup>5</sup>.

The following is quoted from a news item<sup>6</sup>:

*"Oil industry experts estimate that relocating the Pandacan Terminal to a new location, assuming that other local government units would welcome it, would cost the Big Three from Ph 1-2 to 10 billion to acquire or lease a new land, dismantle and relocate the storage tanks for liquid fuels, gaseous LPG and the lubricating oil blending facilities, purchase new tank lorries to feed the new terminal with refinery products, and additional oil and LPG tankers to re-distribute the products from the new terminal to the end-user."*

*As an estimate, replacing the oil pipeline or an oil barge will require an equivalent of over 10-20 tank lorries traversing our Southern Luzon Expressway (SLEX) from the Shell Batangas refinery and Caltex Batangas international terminal as well as our Northern Luzon Expressway (NLEX) from the Petron Bataan Refinery..."*



**Subic-Clark pipeline**<sup>7</sup>

The Subic-Clark pipeline is the oldest oil pipeline in the Philippines.

The Naval Supply Depot (NSD) handled the largest volume of fuel oil of any Navy facility in the world, with more than 4 million barrels of fuel oil processed each month. The depot also supplied Clark Air Base with aviation fuel through a 41 mile (65 kilometers) pipeline. In addition to its fuel operations, NSD also stocked over 200,000 items for use by the fleet<sup>8</sup>.

The pipeline between Porac and Clark was destroyed by lahar flows in the Pasig-Potrero river in 1994 as a result of the Mt. Pinatubo eruption. The rehabilitation included the pumping station at Subic and a tank farm inside Clark. The operation of the pipeline necessarily eliminates the use of trucks in delivering cargo oil to the reservoir inside Clark. Clark has an area of 22 hectares. The Clark depot consists of nine storage tanks with a capacity of 550,000 barrels. The depot is also equipped with a 50,000 barrel jet fuel tank. The rehabilitated pipeline was inaugurated in September 1997.

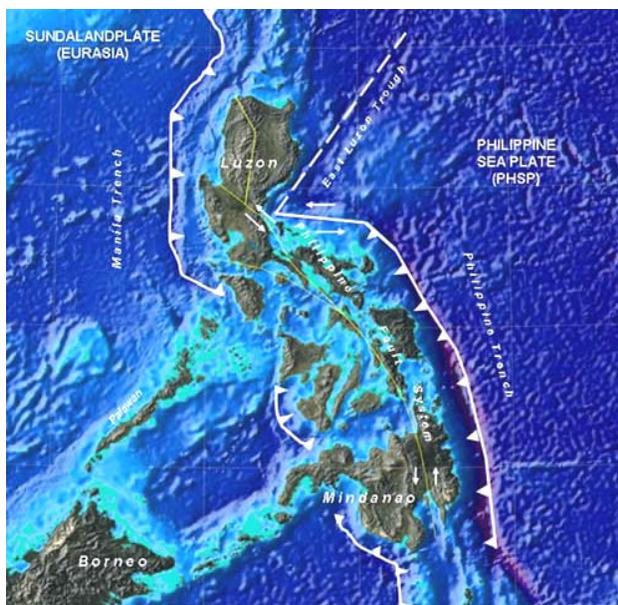
Note that the Subic-Clark pipeline was destroyed by a volcanic eruption, not by an earthquake, neither by bad weather.

<sup>5</sup> <http://www.manilastandardtoday.com/insidebusiness.htm?f=2010/july/15business3.isx&d=2010/ju...>, July 11, 2011

<sup>6</sup> <http://energytechnologyexpert.com/environmental-impacts/633/>, July 11, 2011.

<sup>7</sup> <http://www.margarita-station.com/clarkab.html>, July 9, 2011.

<sup>8</sup> <http://www.preda.org/main/archives/histopry/sbhis07.htm>, July 11, 2011.



### The Philippine fault lines

The Marikina fault, technically known as the Marikina Valley Fault System<sup>9</sup>, is a group of *dextral strike-slip*<sup>10</sup> fault which extends from San Mateo, Rizal to Taguig City in the south; running through the cities of Makati, Marikina, Parañaque, Pasig and Taguig. However, the fault line is much longer, starting from Montalban, San Mateo, Marikina, Pasig, Taguig, Muntinlupa, San Pedro, Binan, Santa Rosa, Calamba, Tagaytay, up to Mindoro Oriental.

Aside from the Marikina fault line, the other fault lines in the Philippines<sup>11</sup> are as follows:

1. Western Philippine fault, that runs from Luzon Sea, Mindoro Strait, Panay Gulf up to the Sulu Sea;
2. Eastern Philippine Fault situated in the Philippine Sea;
3. Southern Mindanao Fault that runs from the Moro Gulf up to the Celebes Sea; and
4. Central Philippine Fault that runs from the entire Ilocos Norte, Aurora, Quezon, Masbate, Eastern Leyte, Southern Leyte, Agusan del Norte, Agusan del Sur, up to Davao del Norte.

According to the Philippine Institute of Volcanology and Seismology (PhilVolcs), the Marikina fault line is potentially the most destructive fault line in the country. If an earthquake with a magnitude of 7 or higher in the Richter scale occurs, it is predicted that the death toll would be as high as 35,000 and injuries of around 120,000, with more than a million people needing evacuation. Furthermore, it cuts through all modern and

progressive portions of Metro Manila such as Eastwood, Rockwell, Ortigas Center, Bonifacio Global City, Ayala Center, and Alabang. It is also the area that educational learning institutions are located like University of the Philippines (Diliman), Ateneo de Manila University, and Mirriam College. The PhilVolcs prediction is ominous – *The Marikina fault line can move anytime because it is already 11 years late for its movement.*

In installing oil pipelines in the Philippines, PhilVolcs data regarding earthquake occurrences should be seriously taken into account.

### Pipeline accidents in the USA

The United States utilized pipelines for a long time now. The Philippines has a lot to learn from more experienced countries. Several accidents occurred between January 2010 to July 2011 due to technical and maintenance problems.

### Conclusion

The proposal to build oil pipelines in the Philippines must consider the following:

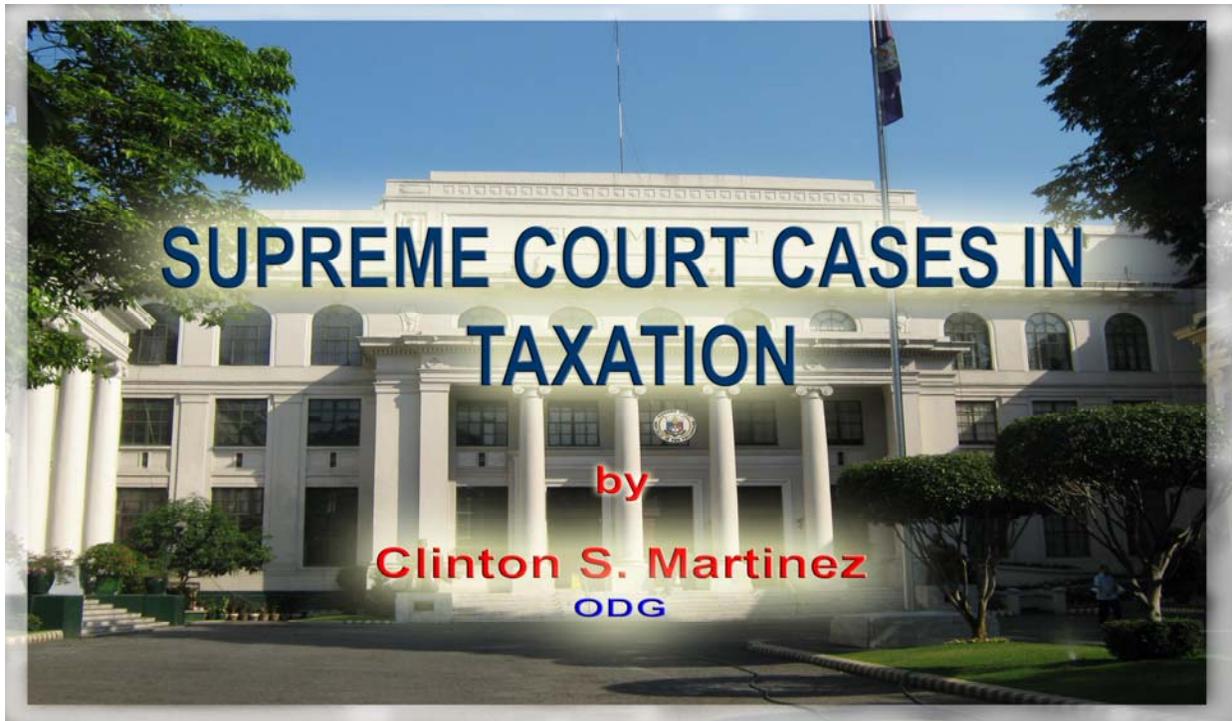
1. The Philippines is earthquake prone. Pipelines are usually underground structures sensitive to any movements of the earth. For example, a pipeline traversing the Marikina fault might prove disastrous in the long run;
2. There are communist rebels in some parts of the country. Pipelines being permanent in nature would be an easy target for them;
3. Pipelines need constant maintenance taking into account the pipeline accidents in the United States. Improper maintenance would result in oil leak, causing damages to health and properties;
4. Aside from the threat of earthquakes, the Philippines is dotted by active volcanoes. Bear in mind that the destruction of the Subic-Clark oil pipeline was due to the eruption of Mount Pinatubo;
5. Pipelines would always pose a threat to the environment;
6. The Philippines is a developing country. Because of this, there is a constant threat of pilferage from people needing "free" fuel.

<sup>9</sup> <http://www.pinoymoneytalk.com/marikina-fault-line/>, July 6, 2011.

<sup>10</sup> Strike-slip fault definition: A type of fault whose surface is typically vertical or nearly so. The motion along a strike-fault is parallel to the strike of the fault surface, and the fault blocks across the fault move sideways past each other. A strike-slip fault in which the block across the fault moves to the right is described as a **dextral strike-slip fault**. If it moves to the left, the relative motion is called **sinistral**. Local deformation near bends in the strike-slip faults can produce pull apart basins and grabens. Flower structures are another by-product of strike-slip faults. A wrench fault is a type of strike-slip fault in which the full surface is nearly vertical.

(Source: [http://www.glossary.oilfield.slb.com/Display.cfm?Term=strike-slip fault](http://www.glossary.oilfield.slb.com/Display.cfm?Term=strike-slip%20fault)), July 8, 2011.

<sup>11</sup> <http://ph.answers.yahoo.com/question/index?qid=20081226041219AhxXOT>, July 10, 2011.



**BRITISH AMERICAN TOBACCO , *Petitioner* vs. JOSE ISIDRO N. CAMACHO, in his capacity as Secretary of the Department of Finance and GUILLERMO L. PARAYNO, JR., in his capacity as Commissioner of the Bureau of Internal Revenue, *Respondents*. PHILIP MORRIS PHILIPPINES MANUFACTURING, INC., FORTUNE TOBACCO, CORP., MIGHTY CORPORATION, and JT INTERNATIONAL, S.A., *Respondents-In-Intervention (En Banc, Consuelo Ynares-Santiago, J. G.R. No. 163583, August 20, 2008).***

**Facts:**

Questioned in this Petition for Review filed by British American Tobacco (BAT), are the legality of the following:

1. Section 145 of the National Internal Revenue Code (NIRC), the Philippine Tax Code, as amended by Republic Act (RA) No. 8424;
2. RA No. 9334, which amended further Sec. 145 of the Tax Code on January 1, 2005;
3. Bureau of Internal Revenue (BIR) Regulations (RR) Nos. 1-97, 9-2003 [Feb. 19, 2003], and 22-2003 [Aug. 13, 2003]; and
4. BIR Memorandum Order (RMO) No. 6-2003 [Mar. 13, 2003].

RA 8240 was issued on January 1, 1997 and amended, among others, Section 142 of the NIRC. RA 8424 renumbered Section 142 as Section 145 of the Tax Code.

Annex “D” of the NIRC, as amended, contains a list of duly registered, existing and active brands of cigarettes in the country. Paragraph (c), Section 145 details four (4) tiers of tax rates based on the net retail price per pack of the cigarettes.

The pertinent provision of said Section provides:

“SEC. 145. *Cigars and cigarettes.* –

“(c) *Cigarettes packed by machine.* - *There shall be levied, assessed and collected on cigarettes packed by machine a tax at the rates prescribed below:*



<sup>1</sup> Tax Reform Act of 1997 (December 11, 1997).

<sup>2</sup> Amends certain provisions of RR No. 1-97 and RR No. 2-97 relative to the excise taxation of alcohol products, cigars and cigarettes for the purpose of prescribing the rules and procedures to be observed in the establishment of the current net retail price of new brands and variants of new brands of alcohol and tobacco products (Source: BIR Website, Oct. 4, 2011).

<sup>3</sup> Implements the revised tax classification of new brands of cigarettes and variants thereof based on the current net retail prices (Source: Supra).

<sup>4</sup> Prescribes the guidelines and procedures on the establishment of current net retail prices of new brands of cigarettes and alcohol products (Supra).

- “(1) If the net retail price (excluding the excise tax and the value-added tax) is above Ten pesos (P10.00) per pack, the tax shall be Thirteen pesos and forty-four centavos (P13.44) per pack;
- “(2) If the net retail price (excluding the excise tax and the value-added tax) exceeds Six pesos and fifty centavos (P6.50) but does not exceed Ten pesos (P10.00) per pack, the tax shall be Eight pesos and ninety-sixty centavos (P8.96) per pack;
- “(3) If the net retail price (excluding the excise tax and the value-added tax) is Five pesos (P5.00) but does not exceed Six pesos and fifty centavos (P6.50) per pack, the tax shall be Five pesos and sixty centavos (P5.60) per pack;
- “(4) If the net retail price (excluding the excise tax and value-added tax) is below Five pesos (P5.00) per pack, the tax shall be One peso and twelve centavos (P1.12) per pack.”

The same Section further states that:

“Variants of existing brands of cigarettes which are introduced in the domestic market after the effectivity of this Act shall be taxed under the highest classification of any variant of that brand.<sup>6</sup>

“New brands shall be classified according to their current net retail price.

“For the above purpose, net retail price shall mean the price at which the cigarette is sold on retail in 20 major supermarkets in Metro Manila (for brands of cigarettes marketed nationally), excluding the amount intended to cover the applicable excise tax and the value-added tax. For brands which are marketed only outside Metro Manila, the net retail price shall mean the price at which the cigarette is sold in five major supermarkets in the region excluding the amount intended to cover the applicable excise tax and value-added tax.

“The classification of each brand of cigarettes based on its average net retail price as of October 1, 1996, as set forth in Annex “D” of this Act, shall remain in force until revised by Congress.”

The BIR issued RR No. 1-97 to implement RA No. 8240. Said RR categorized the existing brands of cigarettes as those duly registered or active brands prior to 1 January 1997. It is further stated that “New brands, or those registered after January 1, 1997, shall be initially assessed at their suggested retail price until such time that the appropriate survey to determine their current net retail price is conducted.” The Supreme Court (SC) cited the following provisions:

“SECTION 2. *Definition of Terms.*

“3. Duly registered or existing brands of cigarettes - shall include duly registered, existing or active brands of cigarettes, prior to January 1, 1997.

“6. *New Brands* - shall mean brands duly registered after January 1, 1997 and shall include duly registered, inactive brands of cigarette not sold in commercial quantity before January 1, 1997.

“Section 4. Classification and Manner of Taxation of Existing Brands, New Brands and Variant of Existing Brands.

“B. New Brands

“New brands shall be classified according to their current net retail price. In the meantime that the current net retail price has not yet been established, the suggested net retail price shall be used to determine the specific tax classification. Thereafter, a survey shall be conducted in 20 major supermarkets or retail outlets in Metro Manila (for brands of cigarette marketed nationally) or in five (5) major supermarkets or retail outlets in the region (for brands which are marketed only outside Metro Manila) at which the cigarette is sold on retail in reams/cartons, three (3) months after the initial removal of the new brand to determine the actual net retail price excluding the excise tax and value added tax which shall then be the basis in determining the specific tax classification. In case the current net retail price is higher than the suggested net retail price, the former shall prevail. Any difference in specific tax due shall be assessed and collected inclusive of increments as provided for by the National Internal Revenue Code, as amended.”

Petitioner BAT, in June 2001, introduced into the field three (3) variants of Lucky Strike: (1) Filter; (2) Lights; and, (3) Menthol Lights with a suggested retail price of P9.90 per pack (Underscoring supplied). Hence, as per the rates

<sup>6</sup> Under the present Tax Code, it is provided: “Variants of existing brands and variants of new brands of cigarettes which are introduced in the domestic market after the effectivity of this Act shall be taxed under the proper classification thereof based on their suggested net retail price: Provided, however, That such classification shall not, in any case, be lower than the highest classification of any variant of that brand.

of the NIRC, as amended, said brands were assessed the excise tax of P8.96 per pack. (Underscoring supplied)

Subsequently, on February 17, 2003, the BIR issued RR No. 9-2003 which amended RR No. 1-97. The former enshrines for a periodic review every two years or earlier, of the current net retail price of new brands and variants in order to establish and update the tax classification<sup>7</sup>.

RMO No. 6-2003, issued March 11, 2003, prescribes the guidelines and procedures in arriving at the prevailing net retail prices of new brands of alcohol products as well as cigarettes. Additionally, RR No. 22-2003 was released on August 8, 2003 with the intent of putting into effect the revised tax classification of some brands put into the market after 1 January 1997, pursuant to the survey of their current net retail price. The census showed that the three brands of Lucky Strike alluded to above had the net retail prices of: (1) P22.54; (2) P22.61; and, (3) P21.23, per pack.

Respondent Commissioner of Internal Revenue (CIR), based on the showing that Lucky Strike's average net retail price is over P10.00 per pack, suggested the rate of P13.44 per pack.

This did not sit well with Petitioner. Hence BAT, on 1 September 2003, filed for an injunction with the court<sup>8</sup> praying for the issuance of a Temporary Restraining Order (TRO) and/or Writ of Preliminary Injunction (Civil Case No. 03-1032), to enjoin the implementation of: (1) Section 145 of the Tax Code; (2) RR No. 1-97; (3) RR No. 9-2003; (4) RR No. 22-2003; and, (4) RMO No. 6-2003 "X x x on the ground that they discriminate against new brands of cigarettes, in violation of the equal protection and uniformity provisions of the Constitution."

In reply, the CIR filed an Opposition.

The RTC, on 2 September 2003, denied the application of BAT for the issuance of a TRO stating that "X x x the courts have no authority to restrain the collection of taxes."

Respondent Secretary of Finance, upon the other hand, filed a Motion to Dismiss, alleging that "x x x the petition is premature for lack of an actual controversy or urgent necessity to justify intervention." This Motion to Dismiss was denied by the RTC in an Order dated 4 March 2004 and, it issued a Writ of Preliminary

Injunction to enjoin the implementation of RR Nos. 1-97, 9-2003, 22-2003 and RMO No. 6-2003. Respondents then filed a Motion for Reconsideration (MR) and Supplemental Motion for Reconsideration. Petitioner and CIR both stipulated that the sole issue in the case is the constitutionality of the questioned law, order and regulations.

The trial court, in a decision dated 12 May 2004, dismissed the Petition for lack of merit, upholding the constitutionality of the questioned issuances. It also lifted the writ of preliminary injunction.

BAT appealed the case to the SC on a pure question of law. While said petition was pending, RA No. 9334<sup>9</sup> took effect on January 1, 2005.

#### Issues:

**Procedural.** - (1) Whether BAT should have brought the action before the Court of Tax Appeals (CTA) and not the RTC. (2) Whether BAT is estopped from questioning the authority of the CIR.

**Substantive.** - (1) Whether Section 145 of the NIRC is constitutional. (2) Whether the RRs are invalid insofar as they empower the BIR to reclassify or update the classification of new brands of cigarettes based on their current net retail prices every two years or earlier. (3) Whether RA 8240, as amended by RA 9334 and its IRRs violate the General Agreement on Tariffs and Trade (GATT) of 1947.

#### Held:

**Questions on Procedure.** -

**On Jurisdiction.** - Under RA No. 1125, as amended, the jurisdiction of the CTA is spelled-out in Section 7. In declaring that BAT properly filed the case with the RTC, the SC said:

*"While the x x x statute confers on the CTA jurisdiction to resolve tax disputes in general, this does not include cases where the constitutionality of a law is challenged. Where what is assailed is the validity or constitutionality of law, or a rule or regulation issued by the administrative agency in the performance of its quasi-legislative function, the regular courts have*

<sup>7</sup> The SC decision provides: "For the purpose of establishing or updating the tax classification of new brands and variants(s) thereof, their current net retail price shall be reviewed periodically through the conduct of survey or any other appropriate activity, x x x, every two (2) years unless earlier ordered by the Commissioner. However, notwithstanding any increase in the current net retail price, the tax classification of such new brands shall remain in force until the same is altered or changed through the issuance of an appropriate Revenue Regulations."

<sup>8</sup> Regional Trial Court (RTC) of Makati, Branch 61.

<sup>9</sup> (1) "increased the excise tax rates provided in paragraph ( c ) of Section 145; (2) mandated that new brands of cigarettes shall initially be classified according to their suggested net retail price, until such time that their correct tax bracket is finally determined under a specific period and, after which, their classification shall remain in force until revised by Congress; (3) retained Annex 'D' as tax base of those surveyed as of October 1, 1996 including the classification of brands for the same products which, although not set forth in said Annex 'D,' were registered on or before January 1, 1997 and were being commercially produced and marketed after the effectivity of this Act. Said classification shall remain in force until revised by Congress; and (4) provided a legislative freeze on brands of cigarettes introduced between the period January 2, 1997 to December 31, 2003, such that said cigarettes shall remain in the classification under which the BIR has determined them to belong as of December 31, 2003, until revised by Congress."

jurisdiction to pass upon the same. X x x. Indeed, the Constitution vests the power of judicial review or the power to declare a law, treaty, international or executive agreement, presidential decree, order, instruction, ordinance, or regulation in the courts, including regional trial courts.”

**On Estoppel.** - The SC declared that BAT is not guilty of violating the principle of estoppel. The Court said:

“We find that petitioner was not guilty of estoppel. When it made the undertaking to comply with all issuances of the BIR, which at that time it considered as valid, petitioner did not commit any false misrepresentation or misleading act. Indeed, petitioner cannot be faulted for initially undertaking to comply with, and subjecting itself to the operation of Section 145(C), and only later on filing the subject case praying for the declaration of its unconstitutionality when the circumstances change and the law results in what it perceives to be unlawful discrimination. The mere fact that a law has been relied upon in the past and all that time has not been attacked as unconstitutional is not a ground for considering petitioner stopped from assailing its validity. For courts will pass upon a constitutional question only when presented before it in bona fide cases for determination, and the fact that the question has not been raised before is not a valid reason for refusing to allow it to be raised later.”

On Substantive Matters. –

**On the constitutionality of Section 145,** the SC declared:

“X x x, the central issue is whether or not the classification freeze provision violates the equal protection and uniformity of taxation clauses of the Constitution.”

“X x x. The applicable standard to avoid the charge that there is denial of this constitutional mandate whether the assailed act is in the exercise of the police power or the power of eminent domain is to demonstrate ‘that the governmental act assailed, far from being inspired by the attainment of the common weal was prompted by the spirit of hostility, or at the very least, discrimination that finds no support in reason. It suffices then that the laws operate equally and uniformly on all persons under similar circumstances or that all persons must be treated in the same manner, the conditions not being

different, both in the privileges conferred and the liabilities imposed. X x x. Hence the constant reiteration of the view that classification if rational in character is allowable. X x x.

“RA 8240 was the first of three parts in the Comprehensive Tax Reform Package then being pushed by the Ramos Administration. It was enacted with the following objectives stated in the Sponsorship Speech of Senator Juan Ponce Enrile (Senator Enrile), viz:

“First, to evolve a tax structure which will promote fair competition among the players in the industries concerned and generate buoyant and stable revenue for the government.

“Second, to ensure that the tax burden is equitably distributed not only amongst the industries affected but equally amongst the various levels of our society that are involved in various markets that are going to be affected by the excise tax on distilled spirits, fermented liquor, cigars and cigarettes.

“In the case of firms engaged in the industries producing the products that we are about to tax, this means relating the tax burden to their market share, not only in terms of quantity, x x x, but in terms of value.

“In case of consumers, this will mean evolving a multi-tiered rate structure so that low-priced products are subject to lower rates and higher-priced products are subject to higher tax rates.

“Third, to simplify the tax administration and compliance with the tax laws that are about to unfold in order to minimize losses arising from inefficiencies and tax avoidance scheme, if not outright tax evasion.

“All in all, the classification freeze provision addressed Congress’s administrative concerns in the simplification of tax administration of sin products, elimination of potential areas for abuse and corruption in tax collection, buoyant and stable revenue generation, and ease of projection of revenues. Consequently, there can be no denial of the equal protection of the laws since the rational-basis test is amply satisfied.

“The Constitution presumes that, absent some reason to infer antipathy, even improvident decisions will eventually be rectified by the democratic process, and that judicial intervention is generally unwarranted no matter how

*unwisely we may think a political branch has acted. Thus, we will not overturn such a statute unless the varying treatment of different groups or persons is so unrelated to the achievement of any combination of legitimate purposes that we can only conclude that the legislature's actions were irrational.*" (Underscoring provided)

**On the Validity of the RRs and RMO**, the SC pronounced that:

*"In sum, Section 4(B)(e)(c), 2<sup>nd</sup> paragraph of Revenue Regulations No. 1-97, as amended by Section 2 of Revenue Regulations 9-2003, and Sections II(1)(b), II(6), II(7), III (Large Tax Payers Assistance Division II) II(b) of Revenue Memorandum Order No. 6-2003, as pertinent to cigarettes packed by machine, are invalid insofar as they grant the BIR the power to reclassify or update the classification of new brands every two years or earlier. Further, these provisions are deemed modified upon the effectivity of RA 9334 on January 1, 2005 insofar as the manner of determining the permanent classification of new brands is concerned."* (Emphasis supplied)

**On the question as to whether the GATT has been violated**, the SC opined:

*"The classification freeze provision uniformly applies to all newly introduced brands in the market, whether imported or locally manufactured. It does not purport to single out imported cigarettes in order to unduly favor locally produced ones. Further, petitioner's evidence was anchored on the alleged unequal tax treatment between old and new brands which involves a different frame of reference vis-à-vis local and imported products. Petitioner has, therefore, failed to clearly prove its case, both factually and legally, within the parameters of the GATT.*

*"At any rate, even assuming arguendo that petitioner was able to prove that the classification freeze provision violates the GATT, the outcome would still be the same. The GATT is a treaty duly ratified by the Philippine Senate and under Article VII, Section 21 of the Constitution, it merely acquired the status of a statute. Applying the basic principles of statutory construction in case of irreconcilable conflict between statutes, RA 8240, as amended by RA 9334, would prevail over the GATT either as a later enactment by Congress or as a special law*

*dealing with the taxation of sin products."*

The SC concludes:

*"WHEREFORE, the petition is PARTIALLY GRANTED and the decision of the Regional Trial Court of Makati, Branch 61, in Civil Case No. 03-1032, is AFFIRMED with MODIFICATION. As modified, this Court declares that:*

*(1) Section 145 of the NIRC, as amended by Republic Act No. 9334, is CONSTITUTIONAL; and that*

*(2) Section 4(B)(e)(c), 2<sup>nd</sup> paragraph Revenue Regulations No. 1-97, as amended by Section 2 of Revenue Regulations 9-2203, and Sections II(1)(b), II(4)(b), II(7), III (Large Tax Payers Assistance Division II) II(b) of Revenue Memorandum Order No. 6-2003, insofar as pertinent to cigarettes packed by machine, are INVALID insofar as they grant the BIR the power to reclassify or update the classification of new brands every two years or earlier."*



**2. HON. SECRETARY OF FINANCE AND HON. GUILLERMO L. PARAYNO, JR., in his capacity as COMMISSIONER OF INTERNAL REVENUE, Petitioners, vs. LA SUERTE CIGAR AND CIGARETTE FACTORY, TELENGTAN BROTHERS & SONS, INC., Respondents (Ynares-Santiago, J. G.R. No. 166498, June 11, 2009).**

**Facts:**

*Assailed in this Petition is the July 12, 2004 Decision of the Regional Trial Court (RTC) of Paranaque City<sup>10</sup> "X x x declaring as void Revenue Regulations Nos. 9-2003 and 22-2003 insofar as they authorize the Bureau of Internal Revenue (BIR) to periodically conduct a survey on the current net retail prices of cigarettes registered after January 1, 1997 for the purpose of their tax classification."*

<sup>10</sup> Civil Case No. 03-0117.

The pertinent Section of the National Internal Revenue Code (NIRC)<sup>11</sup>, as amended, provides:

“Sec. 145. Cigars and Cigarettes<sup>12</sup>. –

“(C) Cigarettes Packed by Machine. - There shall be levied, assessed and collected on cigarettes packed by machine a tax at the rates prescribed below:

“(1) If the net retail price (excluding the excise tax and the value-added tax) is above Ten pesos (P10.00) per pack, the tax shall be Twelve pesos (P12.00) per pack; [P13.44 effective January 1, 2000]

“(2) If the net retail price (excluding the excise tax and the value-added tax) exceeds Six pesos and fifty centavos (P6.50) but does not exceed Ten pesos (P10.00) per pack, the tax shall be Eight pesos (P8.00) per pack; [P8.96 effective January 1, 2000]

“(3) If the net retail price (excluding the excise tax and the value-added tax) is Five pesos (P5.00) but does not exceed Six pesos and fifty centavos (P6.50) per pack, the tax shall be Five pesos (P5.00) per pack; [P5.60 effective January 1, 2000]

“(4) If the net retail price (excluding the excise tax and the value-added tax) is below Five pesos (P5.00) per pack, the tax shall be One peso (P1.00) per pack. [P1.12 effective January 1, 2000]”

Effective January 1, 2000, the above rates shall be increased by twelve percent (12%). Annex “D” of the NIRC contains the result of a survey of the net retail prices per pack of cigarettes as of October 1, 1996. It also classified existing brands as those registered and existing prior to January 1, 1997, which classification cannot be revised except by legislative fiat. Revenue Regulations (RR) No. 1-97 was issued by the Bureau of Internal Revenue (BIR) to implement the provisions of RA No. 8240. Said RR provided that new brands, or those registered after January 1, 1997, shall be initially assessed at their suggested retail prices. Moreover, it is provided therein that “Duly registered or existing brand of cigarette – shall include duly registered, existing or active brands of cigarettes, prior to January 1, 1997.” [Sec. 2, Definition of Terms (3)]

Other important portions of the RR cited by the Supreme Court (SC) are:

“6. **New Brands - shall mean duly registered after January 1, 1997 and shall include duly registered, inactive brands of cigarettes not sold in commercial quantity before January 1, 1997.**

“Section 4. Classification and Manner of Taxation of Existing Brands, New Brands and Variant of Existing Brands.

“B. New Brand

“**New brands shall be classified according to their current net retail price. In the meantime that the current net retail price has not yet been established, the suggested net retail price shall be used to determine the specific tax classification. Thereafter, a survey shall be conducted in 20 major supermarkets or retail outlets in Metro Manila (for brands of cigarette marketed nationally) or in five (5) major supermarkets or retail outlets in the region (for brands which are marketed only outside Metro Manila) at which the cigarette is sold on retail in reams/cartons, three (3) months after the initial removal of the new brand to determine the actual net retail price excluding the excise tax and value added tax which shall then be the basis in determining the specific tax classification. In case the current net retail price is higher than the suggested net retail price, the former shall prevail. Otherwise, the suggested net retail price shall prevail. Any difference in specific tax due shall be assessed and collected inclusive of increments as provided for by the National Internal Revenue Code, as amended. (Emphasis supplied)**”

Astro and Memphis cigarettes together with their variants, were entered into the market by respondents on February 1999, with suggested net retail prices of below P5.00 per pack and a temporary excise tax pegged at P1.00 per pack. Subsequently (May 15, 1999), respondents requested the BIR to conduct the survey to find out the final tax classification of Astro and Memphis. The BIR, in a reply by Assistant Commissioner Leonardo B. Albar dated June 24, 1999, “X x x informed respondents that based on the survey conducted by the BIR for purposes of determining the official and final tax classification, the specific tax of Astro and Memphis cigarettes is P1.00. The survey showed that the average net retail prices per pack of said cigarettes is below P5.00, hence, the corresponding excise tax under Section 145(C) (4) is P1.00 per pack. This was increased to P1.12 per pack, pursuant to the 12% tax rate increase under Section 145 of the NIRC, effective January 1, 2000.”

<sup>11</sup> Republic Act (RA) No. 8240 took effect on January 1, 1997. RA No. 8424 was subsequently passed recodifying the Tax Code and Section 142 was renumbered as Section 145.

<sup>12</sup> The rates have been revised under the present NIRC.

The BIR issued on February 17, 2003 the Questioned RR No. 9-2003 which amended RR No. 1-97. Section 4(B)(e)(c), 2<sup>nd</sup> paragraph of RR No. 1-97, as amended by RR No. 9-2003, provides:

*“For the purpose of establishing or updating the tax classification of new brands and variant(s) thereof, their current net retail price shall be reviewed periodically through the conduct of survey or any other appropriate activity, as mentioned above, every two (2) years unless earlier ordered by the Commissioner. However, notwithstanding any increase in the current net retail price, the tax classification of such new brands shall remain in force until the same is altered or changed through the issuance of an appropriate Regulation Regulations.”*

The pertinent portion of RR 9-2003 reads:

*“SEC. 4. TRANSITORY CLAUSE. - For all brands duly registered and introduced in the market beginning January 1, 1997 the current net retail price of which was not determined for the last two (2) years from effectivity hereof, a determination or re-determination of the current net retail prices thereof shall be conducted immediately upon the effectivity of these Regulations.”*

RR No. 22-2003 was subsequently issued on August 8, 2003 to put into effect the revised tax classification of some new brands introduced in the market after January 1, 1997. This was based on the mandate of RR 9-2003. Annex “A” of RR No. 9-2003 contains the outcome of the survey that the average net retail prices of Astro and Memphis is from P5.72 to P6.13, which increased the excise tax from P1.12 per pack to P5.50 per pack.

The dispositive part of the trial court decision states:

*“WHEREFORE, finding RR Nos. 9-2003 and 22-2003 not in conformity with Section 145 in relation to Section 244 of the Tax Code as they tend to infringe upon the legislative power of taxation, and therefore violative of the constitutional provision that tax laws should originate from Congress, the same are hereby declared unconstitutional and ineffective and as such, the defendants Secretary of Finance and Commissioner of Internal Revenue are hereby permanently enjoined from implementing thereof insofar as they required re-determination and re-classification of Astro and Memphis brands and their variants for purposes of computing excise tax on such products.”*

**Issue:**

Whether the BIR has the power to periodically review or re-determine the current net retail prices of new brands for the purpose of updating their tax classification as per RR Nos. 9-2003 and 22-2003.

**Held:**

The Supreme Court (SC) ruled in favor of the respondents. The SC elucidated:

*“The issue has been settled in the recent case of British American Tobacco v. Camacho where the Court held, among others, that Revenue Regulations Nos. 9-2003, 22-2003, and Revenue Memorandum Order No. 6-2003, as pertinent to cigarettes packed by machine, are invalid insofar as they grant the BIR the power to reclassify or update the classification of new brands every two years or earlier.*

*“Upon their launch, new brands shall be initially taxed based on their suggested net retail price. Thereafter, a survey shall be conducted within three (3) months to determine their current net retail prices and, thus, fix their official tax classifications. However, the BIR made a turnaround by issuing Revenue Regulations No. 9-2003, dated February 17, 2003, which partly amended Revenue Regulations No. 1-97, by authorizing the BIR to periodically reclassify new brands (i.e., every two years or earlier) based on their current net retail prices. Thereafter, the BIR issued Revenue Memorandum Order No. 6-2003, dated March 11, 2003, prescribing the guidelines on the implementation of Revenue Regulations No. 9-2003. This was patent error on the part of the BIR for being contrary to the plain text and legislative intent of RA 9240.*

*“The reclassification of Astro and Memphis pursuant to Revenue Regulations Nos. 9-2003 and 22-2003 constitutes the prohibited reclassification contemplated in British American Tobacco v. Camacho. It will be recalled that these brands were already classified by the BIR based on their current net retail prices in 1999 through a market survey. Consequently, their upward reclassification in 2003 by the BIR through another market survey is a prohibited reclassification.*

*“Contrary to petitioners’ contention, the above classification of Astro*

and Memphis cigarettes is valid. The revenue regulations then in force merely required that the concerned taxpayer be notified of the result of the market survey which is then used as basis for fixing the official and final tax classification of a new brand. This has been sufficiently satisfied by the letter of the

Assistant Commissioner, hence, the fact that the same was not in the form of a numbered ruling will not invalidate the classification contained therein.”

The petition was denied.



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 Website: <http://www.senate.gov.ph>  
 Email: [attydascil@yahoo.com](mailto:attydascil@yahoo.com), [taxbits@yahoo.com](mailto:taxbits@yahoo.com)  
 Telefax No.: 552-6849 ; Tel. No. : 552-6850

**Editors and Contributing Writers**

**Atty. RODELIO T. DASCIL, MNSA**  
 Director General

**Atty. EMMANUEL M. ALONZO**  
 Director III, Legal & Tariff

**RECHILDA B. GASCON, MNSA**  
 Director III, Tax Policy & Admin

**MARIA LUCRECIA R. MIR, MNSA**  
 Director III, Direct Taxes

**VIVIAN A. CABILING**  
 Director III, Indirect Taxes

**JULIETA M. FONTIVEROS**  
 Director II, Legal & Tariff

**NORBERTO M. VILLANUEVA**  
 Director II, Tax Policy & Admin

**ELVIRA P. CRUDO**  
 Director II, Direct Taxes

(Vacant)  
 Director II, Indirect Taxes

**CLINTON S. MARTINEZ**  
 LSO-I, ODG

**BONIFACIO R. JOSON**  
 LSA-III, ODG - Layout Artist

The Articles were principally prepared by the authors, under the supervision of STSR Directors and the overall guidance of its Director-General. The views and opinions expressed are those of STSR and do not necessarily reflect those of the Senate, its leadership, or its individual members. For comments and suggestions, please email us at [attydascil@yahoo.com](mailto:attydascil@yahoo.com), or [taxbits@yahoo.com](mailto:taxbits@yahoo.com).