

**COMMISSIONER OF INTERNAL REVENUE, PETITIONER, VS.
ARMANDO L. ABAD, DOING BUSINESS UNDER THE TRADE NAME OF
REPUBLIC ALCOHOL DISTILLERY, AND THE COURT OF TAX
APPEALS, RESPONDENTS.**

G.R. No. L-19627. June 27, 1968

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CASTRO, J.;

The respondent Armando L. Abad, doing business under the name Republic Alcohol Distillery, is a manufacturer and seller of denatured alcohol. On August 14, 1958 he applied for the denaturation of 33,000 gauge liters of rectified alcohol, upon the following formula prescribed by regulation of the Bureau of Internal Revenue:

"To every one hundred (100) liters of ethyl alcohol of not less than 180 degrees proof, there shall be added two (2) liters of methanol and one-half (1/2) liter of pyridine."

His application was granted. So on August 21 a denatur-ing committee from the BIR went to his warehouse in Grace Park, Caloocan, Rizal to supervise the denaturation of the alcohol.

In a surprise inspection made of the respondent's establishment on August 25, 1958, however, a team of BIR inspectors found that the alcohol had not been completely denatured and that it could still be used for compounding liquors. The team also discovered that 22,580 gauge liters had been removed from the respondent's warehouse and sold, and only 10,480 gauge liters were left.

On September 2, 1958 the petitioner Commissioner of Internal Revenue demanded from the respondent the payment of 19, 204.20 as specific tax on 22,580 gauge liters of alcohol plus P10,000 as compromise penalty. Three days later the 10,480 gauge liters of alcohol was again denatured to make it conform to the BIR formula for denatured alcohol.

Domestic alcohol, when denatured and used for industrial purposes, is exempt from the payment of specific tax.[1] In the case at bar, the petitioner insisted on the assessment of the tax on the basis of a finding that the respondent's alcohol had not been completely denatured so as to render it unfit for human consumption, citing a laboratory examination made by the National Bureau of Investigation which showed that the alcohol could still be used for making Chinese wines "without immediate danger to consumer."

The Tax Court did not find it necessary to pass on this point. In its view no liability for the removal of the alcohol could be imputed to the respondent as the whole process of denaturation was undertaken by a committee of the BIR without the intervention of the respondent. If the alcohol had not in fact been completely denatured, the blame should be laid on the denaturing committee over which "[the respondent] had no control," as indeed it would be unjust to make him liable for its negligence. Said the Tax Court:

"Samples of the denaturants were taken from [the respondent's] bonded denaturing warehouse by a BIR employee, Mr. Manuel Cariñgal, and brought to the BIR Laboratory Section for analysis (p. 79, t. s. n.) and the reports of analysis were duly accomplished (Exhibits E-1, E-2 and E-3), showing that the denaturants passed

the commercial grade and could be used for denaturing (pp. 80-82, t.s.n.). Upon receipt of the Laboratory analysis reports on the denaturants, the Chief, Alcohol Tax Division, pursuant to Memorandum Order No. V-799 of the Bureau of Internal Revenue, dated January 29, 1958, directed the Denaturing Committee, composed of Mr. Marcelino de Leon, Chairman, and Drug Inspector Mercedes Ylagan and Mr. Inocencio Gonzales, Jr., Chief, Laboratory Section, Members, who are all internal revenue officers, to proceed on August 21, 1958 to the bonded denaturing warehouse of the petitioner at Grace Park, Caloocan, Rizal and to denature the 33,000 gauge liters of rectified ethyl alcohol of [the respondent]. The Denaturing Committee denatured the rectified alcohol of the [respondent] in accordance with the standard procedures prescribed by the internal revenue law and regulations (please see testimony of Mr. Marcelino de Leon, pp. 27-77, t.s.n., and testimony of Mr. Inocencio Gonzales, Jr., pp. 77-98, t.s.n.), and after the denaturation the said Denaturing Committee took, through the manholes on top of the three denaturing tanks used in the denaturation, two samples from each of the three tanks and sealed the said samples, on which seals were affixed the signature of the members of the Denaturing Committee and that of the resident manager of the bonded denaturing plant. One set of the samples was left at the denaturing plant and the other set was taken by the Denaturing Committee to the Laboratory Section of the Bureau of Internal Revenue for analysis. After the denaturation and before leaving the premises, the Denaturing Committee duly sealed all the openings of the denaturing tanks. The quantity of the rectified alcohol and the denaturants used in denaturation were duly entered in the Official Register Book of the denaturing plant (Exhibit 1) by the BIR storekeeper-gauger and the resident manager of the plant, and the members of the Denaturing Committee accomplished the requisite certificates of denaturation (Exhibits G, G-1 and C-2). The samples of the denatured alcohol taken by the Denaturing Committee were brought to the BIR Laboratory Section and upon analysis, were found to be duly denatured. (p. 91, t.s.n.)."

The Petitioner assails these findings. It is not true, he argues, that the respondent had no hand in the denaturation of his alcohol. "The process of denaturing had its inception from the time the respondent filed with the bureau of Internal Revenue his application to denature alcohol and said process is a Continuing single act, including all its other incidents, such as the analysis and identification of the denaturants, the accomplishment of the covering report of the Denaturing Committee, and the making of the entries in the books of the respondent. Moreover, the respondent owns the denaturing plant and holds the keys to the plant and its various rooms and compartments (pp. 107, 108); his employees and laborers provide the rectified alcohol and the denaturants to the Denaturing Committee and keep and make the entries in the books and other records required by the law and regulations governing the denaturation of alcohol. (Pp. 11, 115, 122, 123, t.s.n.) Certainly, the respondent cannot absolutely divorce himself from all these intricately interwoven acts and claim that he had nothing to do with the denaturing process." [2] Indeed, the claim is made that there is no evidence to show that the denaturants used by the committee on August 21, 1958 were the same ones which the day before had been analyzed and found satisfactory for the purpose, thereby insinuating that there had been a substitution made. [3]

After analyzing the entire evidence we think that, on the whole, the Tax Court's findings as to the steps taken in the denaturation of the alcohol are correct. Thus it appears that before the actual process of denaturation was begun, a BIR agent took samples of the denaturants for analysis and then sealed the containers by affixing a label signed by the chief of the alcohol and prohibited drugs division of the BIR. Carbon copies of these labels were presented in evidence (exhibits F, F-1 and F-2), but the petitioner claims that it was possible that the labels which the denaturing committee found attached to the containers were not the originals of those presented since the chairman of the committee admitted that he did not see the labels when they were typewritten and that blank forms of these labels were available to anyone in the BIR.

The fact remains, however, that the denaturing committee found the containers properly sealed, with the labels intact (the labels were duly signed), and it was not until the committee members had satisfied themselves that the contents were really methanol and pyridine did they begin the process of denaturation.

What is more, according to the evidence,[4]the denaturants were stored in a room in the warehouse as required by revenue regulations, the key to which was held solely by the BIR storekeeper assigned to the respondent's establishment. The respondent had no key to this room, for while the door of the warehouse had two padlocks, the two keys to which were each held by the respondent and the BIR storekeeper, only the BIR storekeeper had a key to the room inside the warehouse. It was in this room that the denaturants were stored after samples had been taken for laboratory analysis. It was also in this room that the BIR denaturing committee found the denaturants on August 21, 1958.

Indeed the petitioner's suspicion that there was a substitution of the denaturants after samples thereof were taken is not borne out by the evidence, and we think that, in the absence of proof to the contrary, the presumption of regularity in the performance of official function, let alone the rule making findings of fact of the Tax Court, when supported by substantial evidence, conclusive, should not be overthrown on slender grounds resting solely on innuendoes and mere say-so.

This is not to say, however, that the respondent is not liable for the specific tax because the truth of the matter is that despite the fact that the procedure outlined in the revenue regulations[5] was ostensibly followed, and despite the certification of the BIR denaturing committee, a subsequent analysis showed that the alcohol in question had not been completely denatured such that it could still be used to make Chinese wines "without immediate danger to consumer." [6]

In an effort to discredit this finding, the respondent claims that the samples taken were unreliable because they were taken from the faucet at the bottom of the tank instead of from the manhole at the top.[7] This claim has no merit. First, the entire mixture was supposed to be denatured alcohol; it should therefore make no difference whether samples were taken from the faucet or from the manhole. The samples taken and analyzed could not have been any less completely denatured than the alcohol that had been drawn from the outlet pipe near the faucet and sold to the respondent's customers. Second, the respondent claims that the standard procedure is to take samples from the manhole, but he has not cited any provision of the revenue regulations prescribing such procedure. Third, if the alcohol in question had been completely denatured, there would have been no need to denature it further. The fact is that because of the insufficient quantity of denaturants, 100 gauge liters of methanol and 25 gauge liters of pyridine had to be added to the remaining 10, 480 liters of alcohol which the BIR investigating team found.[8]

The alcohol was certified as denatured by a BIR committee. It was found not completely denatured in a subsequent examination. Why this was so can only be conjectured. But one thing is certain-- the BIR denaturing committee fell on its job. This is not the first case brought to this Court in which a denaturing committee of the BIR was found remiss in the performance of its duty. In *Central Azucarera de Tarlac v. Collector of Internal Revenue*, [9] alcohol which a BIR denaturing committee had certified as duly denatured was subsequently found to be in fact rectified alcohol and so its owner was held liable for the specific tax.

["]As a licensed manufacturer of rectified and denatured alcohol, the petitioner is responsible for the quality of its products. It cannot escape responsibility by passing it over to the Denaturing Committee concerned primarily with the prevention of frauds on the revenue. The petitioner should have complied with the law and regulations bearing on the denaturation of alcohol.

"[T]he fact that the alcohol in the instant case had been passed upon and certified to by the Denaturing Committee as duly denatured, does not exempt the petitioner from paying the specific tax. It is a cardinal principle of law and well settled in jurisprudence that the government is not estopped by the neglect or omission of its officers or agents . . . "[10]

The Tax Court distinguished *Central Azucarera* from the case at bar, stating that in that case the owner was

represented in the denaturing committee whereas in this case the respondent did not have any participation in the denaturation of the alcohol. And the point is now pressed by the respondent that unlike before when the owner of the alcohol was a member of the denaturing committee, under present BIR regulations the denaturing committee is made up entirely of BIR employees.

Regardless of the composition of the committee, however, the principle laid down in *Central Azucarera* holds true and it is this: the manufacturer is responsible for the quality of his products and he cannot escape this responsibility by showing that the denaturing committee of the BIR has certified his products to be denatured alcohol. The respondent cannot claim ignorance of this principle for indeed the very permit issued to him expressly stated that the manufacture of denatured alcohol should be under his "exclusive responsibility."^[11] This is as it should be, otherwise it would be easy for manufacturers to evade liability on the pre-text that some government official has certified to the quality of their products and that they have every right to rely on this certificate. A contrary rule would encourage irresponsibility on the part of manufacturers, let alone collusions between taxpayers and revenue officials to defraud the public treasury. It is a settled rule of law that in the performance of its governmental functions the State cannot be estopped by the neglect or omission of its agents. Nowhere is this more true than in the field of taxation.

We therefore hold that the respondent Abad is liable for specific tax in the amount of P19,204.20. This liability is unaffected by the probability that the alcohol might have been used for industrial purposes rather than for consumption, because the law specifically provides that specific taxes shall be paid "immediately before removal from the place of production."^[12] It does not matter to what use the article subject to tax is put; the tax attaches from the time the article is removed from the place of production "to be put into the commerce or trade of the country."^[13]

Here the alcohol was sold to customers on various dates between August 21 and August 28, 1958. It was on these dates that the respondent Abad's liability for the tax arose and, therefore, it is from these dates that interest at the legal rate should be paid, pursuant to article 2209 of the Civil Code. The petitioner's demand, contained in his letter of assessment of September 2, 1958, is unnecessary for the purpose of fixing the respondent Abad's liability because the law establishes definite dates for the payment of various taxes. Thus "no room is left for the exercise of purely personal discretion" on the part of revenue officials.^[14] To facilitate the computation of the interest, however, and for purposes of this case under the particular environmental circumstances, we shall consider the last day, August 28, 1958, as the date the entire obligation became due.

With respect to the amount of P10, 000, however, we agree with the respondent that payment thereof cannot be demanded inasmuch as it was offered by the petitioner only by way of compromise and the compromise did not go through. As this Court has had occasions to explain, a compromise implies agreement. One party cannot impose it upon the other. If an offer of compromise is rejected by the taxpayer, as in this case, the Commissioner of Internal Revenue should file a criminal action if he believes that the taxpayer is criminally liable for violation of the tax law as the only way to enforce a penalty.^[15] A penalty can be imposed only on a finding of criminal liability.

ACCORDINGLY, the judgment appealed from is reversed, and the respondent is ordered to pay the petitioner the amount of P19,204.20 as specific tax, with interest at the rate of 6 per cent per annum from August 28, 1958, the date of the last sale. Costs against the respondent.

Concepcion, C.J., Reyes, J.B.L., Dizon, Makalintal, Zaldivar, Sanchez, Angeles, and Fernando, JJ., concur.

[1] Nat. Int. Rev. Code sec. 128: "Exemption in favor of domestic denatured alcohol. - Domestic alcohol of not

less than one hundred eighty degrees proof (ninety per centum absolute alcohol) may, when denatured, be withdrawn from a registered distillery or bonded warehouse without the prepayment of the specific tax prescribed in section 133, for the purpose of being used for fuel, or light, or for use generally in the arts, industries, hospitals, sanitariums, and clinics, or for research or experimental purposes, or for the official use of the Government of the Republic of the Philippines or its instrumentalities or political subdivisions."

[2] Petitioner's brief, 27-28.

[3] See *id.*, 14-17.

[4] *T.s.n.*, pp. 35-36, 85, 108.

[5] A copy of the BIR Circular 16 on denatured alcohol is appended to the brief for the respondent.

[6] Exh. 5.

[7] For an illustration of the tank showing the faucet, man-hole and outlet pipe, see exh. H.

[8] Exh. 2.

[9] 104 Phil. 653 (1958).

[10] *Id.*, 655-56.

[11] Exh. B.

[12] Nat. Int. Rev. Code sec. 124.

[13] See *Asiatic Petroleum Co. v. Rafferty*, 38 Phil. 475, 479 (1918); accord, *Asiatic Petroleum Co. v. Posadas*, 52 Phil. 728 (1929).

[14] *Acoje Mining Co. v. Commissioner of Internal Revenue*, L-19378, March 27, 1968.

[15] See, e.g., *Collector of Internal Revenue v. Pio Barretto Sons, Inc.*, L-11805, May 31, 1960.

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