REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

SECOND DIVISION

PETRON CORPORATION, Petitioner,	**C.T.A. CASE NO. 6136**
	Members:
-versus-	**CASTAÑEDA, JR.,** *Chairperson* **UY,** *and* **PALANCA-ENRIQUEZ,** *JJ.*
COMMISSIONER OF INTERNAL REVENUE, Respondent.	**Promulgated:** AUG 2 3 2006

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DECISION

CASTAÑEDA, JR., J.:

It is an oft-repeated dictum that water cannot rise higher than its source. The Tax Credit Certificates used by the petitioner-assignee to pay its excise taxes did not produce the effect of payment as it has no monetary value even in the hands of the original owners-assignors thereof.

Statement of the Case

This is a petition for review filed by petitioner, Petron Corporation, against the respondent, Commissioner of Internal Revenue, of his assessment and demand for payment of deficiency excise taxes covering the period from the taxable years 1995 to 1997 in the total amount of **SIX**

HUNDRED FIFTY ONE MILLION THREE HUNDRED THIRTY FOUR THOUSAND TWO HUNDRED SIXTY THREE AND 92/100 PESOS (P651,334,263.92), inclusive of the surcharge of P142,195,422.50 and interests of P224,747,996.42, as a result of the cancellation of the Tax Debit Memos issued against the Tax Credit Certificates utilized by petitioner in the payment of its excise taxes.

Statement of Facts

The undisputed facts as culled from the records of the case are as follows:

Petitioner, Petron Corporation, is a corporation organized and existing under and by virtue of Philippine Law, with principal place of business at Petron Mega Plaza, 358 Sen. Gil Puyat Avenue, Makati City. It is a producer of petroleum products and is a Board of Investments (BOI) registered enterprise in accordance with the provision of the Omnibus Investments Code of 1987 (E.O. 226), under Certificates of Registration No. 89-1037 and D95-136. Respondent, on the other hand, is the Commissioner of the Bureau of Internal Revenue (BIR), the government agency tasked, among others, to collect national internal revenue taxes.

During the period covering the years 1994 to 1997, petitioner had been an assignee of several Tax Credit Certificates (TCCs) from various BOI-registered entities (Diamond Knitting Corporation, Filstar Textile Industrial Corporation, Alliance Thread Co., Inc., Fiber Tech. Corporation, Jantex Phils., Inc., and Master Colour System Corporation), for which petitioner utilized in the payment of its excise tax liabilities for the taxable years 1995 to 1997.

Such transfers and assignments of the said TCCs were duly approved by the Department of Finance One-Stop Shop Inter-Agency Tax Credit and Duty Drawback Center (Center), a center which is composed of representatives from the appropriate government agencies, namely: the Department of Finance (DOF), the Board of Investments (BOI), the Bureau of Customs (BOC), and the Bureau of Internal Revenue (BIR).

Petitioner's acceptance and use of the TCCs as payment of its excise tax liabilities for the taxable years 1995 to 1997, had been continuously approved by the DOF, as well as the BIR's Collection Program Division through the issuance of the Tax Debit Memos (TDMs) duly signed by the Assistant Commissioner of the Collection Service of the BIR.

However, on November 15, 1999, respondent issued his assailed "Assessment" against petitioner for deficiency excise taxes, in the total amount of P651,334,263.92, inclusive of surcharges and interests, based on the ground that the TCCs utilized by petitioner in payment of its excise taxes were found by the DOF, pursuant to Excom Resolution No. 03-05-99, to have been fraudulently issued and transferred. In view of this, petitioner, on August 31, 1999 and September 1, 1999, was required by the Center to submit copies of its sales invoices and delivery receipts showing the consummation of the sale transactions to the TCC transferors.

On December 9, 1999, petitioner filed its protest on the "Assessment" issued against it. It argued that the excise taxes as reported in its returns filed were duly paid and the accuracy of such tax returns was never assailed by the respondent; that the subject TCCs were allegedly acquired from qualified recipients thereof and its acquisition was likewise approved by the appropriate government agencies. Moreover, the cancellation of the TDMs was done in violation of petitioner's right to due process considering that the actual cancellation was done without the involvement of petitioner, notwithstanding, that such cancellation was prejudicial to petitioner more than just financially. In its supplemental protest letter dated January 25, 2000, petitioner quoted the case of Petron Corporation vs. Commissioner of Internal Revenue, CTA Case No. 5657, promulgated on July 26, 1999, wherein this Court had resolved the issue of the validity of the TCCs and effectively declared that the cancellation of the TDMs was void and of no effect.

Having received no reply from the respondent, petitioner then elevated this case to this Court on July 10, 2000.

On August 29, 2000, respondent filed his Answer, raising the following as his Special and Affirmative Defenses:

"6. He repleads by reference all the foregoing allegations.

7. The assessment is based on the fact that the Tax Debit Memos (TDMs) issued to petitioner and their related Tax Credit Certificates (TCCs) and TCC transfers, which were used by it in the payment of excise taxes, were cancelled by the Secretary of Finance. With such cancellation, the TDMs and TCCs have no value in money or money's worth and, therefore, the excise taxes for which they were used as payment are now deemed unpaid.

8. The cancellation by the Secretary of Finance of the TDMs and TCCs issued to petitioner and their related TCCs and TCC transfers has the presumption of regularity upon which respondent may validly rely.

9. Prior to the issuance of the assessment, petitioner was informed by the Secretary of Finance of the cancellation of the TDMs issued to it and their related TCCs and TCC transfers, which were used by it in the payment of excise taxes, and the reasons for their cancellation. Since the assessment is based on such cancellation, as stated in the assessment itself, petitioner is deemed to have been

informed of the law and the facts on which the assessment is made in compliance with Section 228 of the Tax Code.

10. Based on the findings of the One-Stop Shop Inter-Agency Tax Credit and Duty Drawback Center of the Department of Finance, the TCCs transferred to petitioner were fraudulently obtained, hence, null and void from the very beginning. Furthermore, the transfers of the TCCs to petitioner were fraudulent since it executed fictitious supply agreements whereby it was made to appear that petitioner delivered fuel to textile mills in consideration for the TCCs when in fact there were no such deliveries.

11. Petitioner used the TCCs fraudulently obtained and fraudulently transferred to it in the payment of excise taxes declared in its excise tax returns with intent to evade tax to the extent of the value represented by the TCCs, thereby rendering the returns fraudulent.

12. Since petitioner filed fraudulent returns with intent to evade tax, the right of the government to asses the tax is ten (10) years from the discovery of the fraud pursuant to Section 222 of the Tax Code.

13. Since petitioner willfully filed fraudulent returns, it is liable for the 50% surcharge and 20% annual interest imposed under Section 248 and 249 of the Tax Code.

14. The government is never estopped from collecting legitimate taxes due to the error committed by its agents (Visayan Cebu Terminal Inc., vs. Commissioner of Internal Revenue, 13 SCRA 257; Tan Guan vs. Court of Tax Appeals, 19 SCRA 903; Atlas Consolidated Mining and Development Corporation vs. Commissioner of Internal Revenue, 102 SCRA 246). The acceptance by the Bureau of Internal Revenue of the TCCs fraudulently obtained and fraudulently transferred to petitioner in the payment of excise taxes turned out to be a mistake. Hence, said payments were void and the excise taxes may be validly collected from petitioner.

15. The assessment was issued in accordance with laws and regulations.

16. All presumptions are in favor of the correctness of tax assessments (Commissioner of Internal Revenue vs. Construction Resources of Asia, Inc., 145 SCRA 671)."

After the parties filed their memoranda, the case was submitted for decision on October 29, 2003.

However, on August 20, 2004, respondent filed an Urgent Motion to Reopen the Case on the ground that additional evidence consisting of documents presented to the Center in support of the TCC transferors' claims for tax credit, as well as documents supporting the applications for approval of the transfer of the TCCs to petitioner, must be presented to prove the fraudulent issuance and fraudulent transfer of the subject TCCs. Respondent submits that it is imperative on his part to do so considering, without necessarily admitting that this instant case is wanting of such evidence, the fate that had befallen upon the respondent in the case of Pilipinas Shell Petroleum Corporation vs. Commissioner of Internal Revenue, CTA Case No. 6003, promulgated on August 2, 2004 wherein this Court held that "there is no clear and convincing evidence that the Tax credit Certificates (TCCs) transferred to Shell (for brevity) and used by it in the payment of excise taxes, were fraudulently issued to the TCC transferors and were fraudulently transferred to Shell."

On September 24, 2004, this Court resolved to grant respondent's motion and thus allowed respondent to present additional evidence in support of his arguments. Subsequent to this Court's Resolution, respondent then filed a Request to Issue Subpoena Ad Testificandum to Ms. Beverly Tañeza-Basman of the Center, and a Subpoena Duces Tecum to the Executive Director or his duly authorized representative, also of the Center.

Petitioner's Motion for Reconsideration filed on October 15, 2004 of the said Resolution was denied by this Court on May 19, 2005 for lack of merit.

After having presented and offered his Supplemental Formal Offer of Evidence on November 21, 2005, and upon the filing of the parties' respective Supplemental Memorandum, this case was finally submitted for decision on April 24, 2006.

STATEMENT OF THE ISSUES

The issues as stipulated by the parties are as follows:

1. Whether Petron's payment of excise taxes from 1995 to 1997, inclusive, thru utilization of the TCCs assigned to it by BOI-registered companies in payment of fuel and petroleum products supplied were valid;

2. Whether the TCCs were fraudulently obtained by the entities/grantees and subsequently fraudulently transferred by them to Petron;

3. Whether Petron was aware of any fraudulence in the obtaining of the TCCs nor of any defect or flaw thereon;

4. Whether the Commissioner of Internal Revenue is estopped from questioning Petron's payment of the TCCs which the BIR continuously approved after the TCCs had been verified and validated by the DOF Center; and

5. Assuming *arguendo* that payments thru utilization of the TCCs were invalid, whether Petron can be held liable for surcharges, interests and other charges.

FINDINGS / DISCUSSION

To better illustrate the issues presented by the parties, provisions of pertinent law, rules and regulations and agreements are hereunder reproduced, to wit:

a. Articles 21 and 39 (k) of the Omnibus Investments Code of 1987

ART. 21. *"Tax Credit"* shall mean any of the credits against taxes and/or duties equal to those actually paid or would have been paid to evidence which a tax credit certificate shall be issued by the Secretary of Finance or his representative, or by the Board, if so delegated by the Secretary of Finance. The tax credit certificates including those issued by the Board pursuant to laws repealed by this Code but without in any way diminishing the scope of the negotiability under their laws of issue ***are transferable under such conditions as may be determined by the Board*** after consultation with the Department of Finance. The tax credit certificate shall be used to pay taxes, duties, charges and fees due to the National Government: *Provided*, That the tax credits issued under this Code shall not form part of the gross income of the grantee/transferee for income tax purposes under Section 29 of the National Internal Revenue Code and are therefore not taxable: *Provided, further*, that such tax credits shall be valid only for a period of ten (10) years from date of issuance."

ART. 39. *Incentives to Registered Enterprises.* – All registered enterprises shall be granted the following incentives to the extent engaged in a preferred area of investment.

xxx xxx xxx

(k) *Tax Credit for Taxes and Duties on Raw Materials.* – Every registered enterprise shall enjoy ***a tax credit equivalent*** **to** the National Internal Revenue ***taxes and Customs duties paid on the supplies, raw materials and semi-manufactured products used in the manufacture***, processing or production of its export products and forming part thereof, exported directly or indirectly by the registered enterprise: *Provided, however*, That the taxes on the supplies, raw materials and semi-manufactured products domestically purchased are indicated as a separate item in the sales invoice. *(Emphasis and underscoring supplied)*

b. Rule VII of the Board of Investment's Rules and Regulations implementing the Omnibus Investments Code

RULE VII. TRANSFERABILITY OF TAX CREDIT CERTIFICATE

Tax credit certificates for taxes and duties that would have been paid on domestic capital equipment purchased, and on raw materials, supplies and semi-manufactured products used in the manufacture, processing or production of its export products and forming part thereof shall be issued by the Secretary of Finance or his representative, or by the Board, if so delegated by the Secretary of Finance."

xxx xxx xxx

Said ***certificate may be transferred in accordance with the memorandum of agreement between the Department of Finance and the Board of Investments*** dated October 5, 1982. However, for tax credits not covered by the said memorandum, i.e., net value earned and net local content tax credit certificate issued under P.D. 1789, as amended, they shall be transferable only to domestic raw material or component suppliers of the registered enterprise. *(Emphasis supplied)*

c. Memorandum between the Department of Finance and Board of Investments, dated October 5, 1982 as amended by DOF-BOI MOA dated August 29, 1985, to implement Article 21 of the Omnibus Investments Code of 1987

Sec. 2. The first three (3) paragraphs of the guidelines contained in the aforementioned Memorandum of Agreement are hereby reworded to read as follows:

1) Henceforth, ***all tax credit certificates***, except for net local content (NLC) and Net Value Earned (NVE), issued to BOI-registered enterprises under EO 226 and PD 1789 as amended BP 391 on or after the effectivity date hereof, ***may be transferred under conditions provided herein***. *(Emphasis and underscoring supplied)*

2) The transferee should be a BOI-Registered firm which is a domestic capital equipment supplier or a raw material and/or component supplier of the transferor.

3) The transferee may apply such tax credit certificate for payment of taxes, duties, charges or fees directly due to the national government for as long as it enjoys BOI incentives under its law of registration.

Sec. 3. All other provisions in the aforementioned Memorandum of Agreement not otherwise amended herein shall continue to have full force and effect.

Sec. 4. The transferability of all tax credit certificates, except those for NLC or NVE, issued to BOI-registered enterprises prior to the effectivity of herein amendments shall continue to be governed by guidelines/conditions existing at the time said certificate mere issued.

d. BOI Letter dated May 15, 1990

During the BOI Board of Investments' meetings of July 27, August 17 and 29, 1990, the following issues regarding transferability of tax credits were clarified and approved:

> 1. Assignee should be a BOI-registered company and at the same time a domestic producer of the raw materials and components being supplied. However, its registration need not be the product that it supplies. The condition that the assignee should be a BOI-registered company shall only apply to the credits issued after January 30, 1990.
>
> 2. Hydraulic oil and penetrating oil shall be classified as supplies in the same manner as diesel fuel oil and industrial gases have been classified and suppliers of the same should be considered as qualified transferees of tax credits.

The first three issues, being interrelated, are hereunder discussed together.

Petitioner submits that the subject TCCs assigned by Alliance Thread Co., Inc., Diamond Knitting Corporation, Fiber Technology Corporation, Filstar Textile Industrial Corporation, Jantex Phils., Inc., and Master Colour System Corporation are all genuine. In fact, petitioner contends that this allegation was never disputed by respondent in his arguments. Petitioner avers that the TCCs were assigned to it in accordance with law and duly approved by appropriate government agencies, as evidenced by the fact that petitioner's utilization of the TCCs in its payment of excise taxes was continuously accepted by the BIR. Moreover, petitioner asserts that it has been faithful in its obligation to issue credit notes to the assignors under the Deeds of Assignment entered into between them, for which these credit notes were availed of by the assignors through the delivery of fuel and other petroleum products upon their order. Such was even confirmed by the audit report of the Court-commissioned Independent Certified Public Accountant, Ms. Lilian S. Linsangan.

Petitioner further avers that there was no fraudulent transfer or assignment of the TCCs nor was there proof that the TCCs were fraudulently obtained by the assignor/transferor companies. Accordingly, the tedious procedure for the assignment of the TCCs, which consist of three layers of review by different government entities, clearly dispels any fraudulent transfer of the TCCs. Moreover, fraud must be established by clear and convincing evidence.

Respondent, on the other hand, is steadfast in his argument that the TCCs were fraudulently obtained by petitioner. Accordingly, a post-audit conducted by the Executive Committee of the Center showed that the assignor-companies did not export at the volume for which they had represented to the Center to obtain the subject TCCs. Thus, the bases for the approval of the TCCs were spurious export documents which effectively render the TCCs void *ab initio*. Further, post-audit revealed that petitioner did not make any deliveries of fuel and other petroleum products to the assignors of the TCCs as agreed upon in their Supply Agreements. Accordingly, petitioner presented evidence to prove that it had delivered fuel products to the TCC transferors/assignors, however, petitioner likewise admitted that some of the fuel products were delivered to other entities other than the transferors/assignors. Pursuant to Rule VII of the Rules and Regulations implementing the provisions of the Omnibus Investments Code of 1997 and the Memorandum of Agreement between the DOF and the BOI, petitioner's non- compliance made the transfer fraudulent.

This Court finds for the respondent.

The first issue involved in this case had already been settled in the case of *Commissioner of Internal Revenue vs. Pilipinas Shell Petroleum*

Corporation, C.T.A. EB No. 64, April 28, 2006, where the Court of Tax Appeals sitting *En Banc* ruled that the subsequent cancellation of the tax credit certificates previously used to pay the assignee's tax liabilities would have the effect of non-payment of the assignee's excise taxes corresponding to the value of the tax credit certificates supposedly used for payment. To quote:

> "At the outset, the DOF findings that the TCCs do not have monetary value is undisputed and was clearly established during the trial proper. Consequently, the effect would be non-payment of respondent's excise taxes corresponding to the value of the TCCs supposedly used for payment. This is so, because payment can only occur if the instrument used to discharge an obligation represented its stated value. A valueless instrument, even if delivered to and accepted by the creditor, not knowing that the same is worthless, would not produce payment. After all, the debtor warrants that his instrument is valid and valuable. Since it was the debtor (respondent) who acquired the subject TCCs from a third party and utilized the same to discharge its own obligations, then respondent must bear the loss".

At this point, it must be stressed that under established procedure, when the Secretary of Finance issues a TCC, notwithstanding compliance of the holder of certain requirements, the same is still subject to re-evaluation. This is unmistakably clear under the express provision as found on the TCCs which states that "This Tax Credit is issued subject to: 1. Post-audit x x x".

It cannot be over-emphasized that the acceptance by the petitioner of the subject TCCs is a contract entered into by and between the issuing authority and the petitioner itself. And as with any other contract, the same is subject to certain conditions binding to both parties. Thus, when petitioner obtained the TCCs, it must have known that it must subject to the conditions as expressly set forth therein. Simply put, it cannot be said that petitioner is unaware of the consequences that may arise after a post-audit is conducted.

Elementary is the rule that the statement on the TCCs stating that it is "subject to a post-audit" is in the nature of a suspensive condition found under Article 1181 of the Civil Code. For expediency:

> Art. 1181. In conditional obligations, the acquisition of rights, as well as the extinguishment or loss of those already acquired, shall depend upon the happening of the event which constitutes the condition.

The above-quoted article speaks of obligations subject to conditions. "These conditions affect obligations in diametrically opposed ways. If the suspensive condition happens, the obligation arises; in other words, if the condition does not happen, the obligation does not come into existence. On the other hand, the resolutory condition extinguishes rights and obligations already existing; in other words, the obligations and rights already exist, but under the threat of extinction upon the happening of the resolutory condition *(8 Manresa 130-131, cited on page 140, Civil Code of the Philippines, Tolentino, 1962 ed., Vol. IV).*

In view of the foregoing provision, this Court rules that the issuance of the tax credit certificate is subject to the suspensive condition of post-audit, wherein post-audit is one which is conducted in order to determine as whether or not the holder of the TCCs is qualified for its issuance. Thus, unless and until there is a final determination of the holder's right to the issuance of the TCCs, there really exists no obligation on the part of the DOF or the BIR to recognize the rights of the holder or transferee/assignee.

Effectively, the post-audit conducted by the Center resulted in a finding of fraud in the transfer of the subject TCCs. Pursuant to Article 39(k) of the

Omnibus Investments Code of 1987, tax credits are granted to BOI-registered entities on taxes and duties paid on raw materials used for the manufacture of their export products. It is therefore a mandatory requirement that claimants for tax credits export their products, as likewise alleged by petitioner. However, the said post-audit conducted on the subject TCCs revealed that the companies to which they were issued did not export at the volume they had represented to the Center, and thus, the basis for the approval of the TCCs were spurious export documents. This conclusion arrived at was grounded on the fact of the amounts of the TCCs are excessively or absurdly higher than the sales of the assignor/transferor-companies. The ratios of the amount of TCCs to the amount of sales, which was computed by dividing the average yearly TCCs by the average yearly sales as indicated in the "Schedule of Tax Credit Certificates/Sales Ratio", were way above the industry average of 13%. It likewise concluded that the transferor/assignor entities could not have exported their registered capacity of yarns and threads considering that from their Audited Financial Statements, their reported cost of machinery and equipment obviously could not produce that much yarn and thread. More so, affidavits from the general managers of the transferor/assignor entities showed that they had no knowledge of any transfer or assignment of the subject TCCs nor were there any deliveries of bunker fuel from petitioner. This clearly shows that the volume of export sales declared to the Center, on the basis of the TCCs issued, were false.

Moreover, post-audit disclosed that there were no deliveries of fuel and other petroleum products from petitioner to the transferor/assignor-companies as stated in their Supply Agreements. This was confirmed by the court-commissioned independent CPA as found in Annex 10 of his report dated March 10, 2003 (*Exhibit A*). In fact, some of the deliveries of the fuel products which were supposed to be for Fiber Technology Corporation were made instead to Filstar Textile Industrial Corporation; those supposed to be delivered to Filstar Textile Industrial Corporation were delivered to Diamond Knitting Corporation and Alliance Thread Co., Inc.; those supposedly for Jantex Phils., Inc. were delivered instead to Diamond Knitting Corporation *(Exhibit "A-15" to "A-15-dd")*. Furthermore, the financial statements of the companies showed that they were not using fuel oil at the levels disclosed to the Center. It must be pointed out that Rule VII of the Rules and Regulations implementing the provisions of the Omnibus Investments Code of 1987 and the Memorandum of Agreement between the DOF and BOI specifically provide that "a TCC transferee should be a domestic capital equipment supplier or a raw material and/or component supplier of the transferor."

The Bureau of Internal Revenue, being a subordinate government agency is bound to adopt the findings of the DOF considering that the latter is the agency which actually conducted the investigations. Under the governing rules, regulations, guidelines and procedures for the application, issuance and transfer of tax credit certificates, the DOF/Center is the competent authority in this respect and when in the conduct of its official mandate, the said authority declaring that certain TCCs are tainted with gross irregularities should be afforded great weight and credit. It cannot be denied that in this instant case, circumstances are abound indicating fraud, both as to the issuance of the subject TCCs, as well as, their transfer to petitioner.

In view of the above and considering that pursuant to the "Liability

Clause" contained in the TCC, wherein both parties, transferor and transferee, are "held jointly and severally liable for any fraudulent act or violation of the pertinent laws, rules and regulations relating to the transfer thereof", petitioner then must suffer the consequences of having fraudulently obtained the TCCs in question. When the petitioner utilized the TCCs in its payment of excise taxes at the time when the post-audit was not yet conducted, it did so at its own risk. Petitioner is therefore liable for the loss of the thing due even if was only caused by the fault of one party and regardless of whether or not there was knowledge on the part of the petitioner of the fraud obtained.

In a nutshell, the validity and propriety of the TCCs in question to effectively constitute payment of the excise taxes due to the national government are still subject to the outcome of the post-audit to be conducted by the Center. Thus, when the issuing authority finds circumstances which may warrant the cancellation of the TCCs, the holder, although it may have allegedly been obtained in good faith, is inevitably bound by the outcome by virtue of the express provisions stated on the TCCs.

Additionally, under Administrative Order No. 266 creating the Center, one of the powers and duties of the Center is to "conduct regular post-audit examination on tax credit certificates issued using standard rates, as well as, to adopt measures and/or penalties to ensure the integrity of the processing and evaluation of tax credit and duty drawback claims." The Executive Committee heading the Center, adopted Resolution No. 03-05-99 prescribing for the guidelines and procedures for the cancellation, recall and recovery of fraudulently issued TCCs. Under the said guidelines, TCCs and TDMs are classified as fraudulent when the "basis for the issuance of the TCCs, TDMs or for the approval of the transfer of a TCC are spurious, tampered, altered and fake commercial and public documents or other acts of gross misrepresentation and deceit employed by the claimant which would give rise to the release of the TCC." And it was through this Resolution No. 03-05-99 that led to the cancellation of the controversial TCCs.

As regards the fourth issue, it is noteworthy to mention that "it is a settled rule of law that in the performance of governmental functions, the State cannot be estopped by the neglect of its agents and officers. Nowhere is this more true than in the field of taxation. *(**Commissioner of Internal Revenue vs. Procter & Gamble Manufacturing Corporation,** No. L- 66838, April 15, 1988).* In stressing the rationale on this settled rule, the Honorable Supreme Court explained that:

> *"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 alcohol should be under his "exclusive responsibility". This is as it should be, otherwise it would be easy for manufacturers to evade liability on the pretext 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 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." (**Commissioner of Internal Revenue vs. Armando L. Abad,** No. L-19627, June 27, 1968)*

Going now to the last issue, in consideration of the fact that no payment took effect because of the cancelled TCCs upon post-audit pursuant to the express terms of the TCCs themselves, petitioner is liable for the deficiency basic excise taxes for the taxable years 1995 to 1997. Nevertheless, this Court finds it necessary to discuss the application of the surcharges and other charges imposed.

With regard to the fifty percent (50%) fraud surcharge, this Court believes that the same should not be imposed. In the case of **Aznar vs. Court of Tax Appeals, 58 SCRA 519**, the Highest Court elucidated this matter, thus:

> *"From the above exposition of facts, we cannot but emphatically reiterate the well established doctrine that fraud cannot be presumed but must be proven. As a corollary thereto, we can also state that fraudulent intent could not be deduced from mistakes however frequent they may be, especially if such mistakes emanate from erroneous entries or erroneous classification of items in accounting methods utilized for determination of tax liabilities. The predecessor of the petitioner undoubtedly filed his income tax returns for the taxable years 1946 to 1951 and those tax returns were prepared for him by his accountant and employees. It also appears that petitioner in his lifetime and during the investigation of his tax liabilities cooperated readily with the B.I.R. and that there is no indication in the record of any act of bad faith committed by him.*
>
> *The lower court's conclusion regarding the existence of fraudulent intent to evade payment of taxes was based merely on a presumption and not on evidence establishing a willful filing of false and fraudulent returns so as to warrant the imposition of the fraud penalty. The fraud contemplated by law is actual and not constructive. It must be intentional fraud, consisting of deception willfully and deliberately done or resorted to in order to induce another to give up some legal right. Negligence, whether slight or gross, is not equivalent to the fraud with intent to evade the tax contemplated by the law. It must amount to intentional wrong-doing with the sole object of avoiding the tax. It necessarily follows that a mere mistake cannot be considered as fraudulent intent, and if both petitioner and respondent Commissioner of Internal Revenue committed mistakes in making entries in the returns and in the assessment, respectively, under the inventory method of determining tax liability, it would be unfair to treat the mistakes of the petitioner as tainted with fraud and those of respondent as made in good*

faith."

Applying the above principle, it can be concluded that petitioner, in the present case, cannot be made to pay the fraud surcharge. It must be emphasized that respondent did not produce evidence to directly prove that there was a willful intention on the part of petitioner to evade the payment of taxes. At the most, petitioner was merely negligent in its acquisition of the controversial TCCs by failing to investigate the validity of the same before obtaining them from the transferor/assignor entities. As the Honorable Supreme Court held, "fraud cannot be presumed but must be proven."

However, petitioner is liable to the Twenty Five percent (25%) late payment surcharge pursuant to Section 248 (A) of the National Internal Revenue Code (NIRC) of 1997. Both the 25% surcharge and the 20% interest per annum imposed under Sections 248 and 249 of the NIRC of 1997 cannot be waived for the same are meant to compensate the government for their inability to utilize the taxes during the time such taxes remain unpaid.

WHEREFORE, premises considered, this instant Petition for Review is hereby **DENIED** for lack of merit. Accordingly, petitioner is **ORDERED TO PAY** the respondent the amount **of FIVE HUNDRED EIGHTY MILLION TWO HUNDRED THIRTY SIX THOUSAND FIVE HUNDRED FIFTY TWO AND 67/100 PESOS (P580,236,552.67),** representing deficiency excise taxes for the taxable years 1995 to 1997, computed as follows:

Basic Tax		P 284,390,845.00
Add:		
Late Payment		
Surcharge (25%)	P 71,097,711.25	
Interest (20%)	224,747,996.42	295,845,707.67
Total		**P580,236,552.67**

In addition, petitioner is **ORDERED TO PAY** the respondent 20% delinquency interest per annum on the P580,236,552.67, computed from December 4, 1999 until the amount is fully paid.

SO ORDERED.

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Associate Justice

WE CONCUR:

ERLINDA P. UY.
Associate Justice

OLGA PALANCA-ENRIQUEZ
Associate Justice

ATTESTATION

I attest that the conclusions in the above Decision were reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Associate Justice
Chairman

CERTIFICATION

Pursuant to Article VIII, Section 13 of the Constitution, and the Division Chairman's Attestation, it is hereby certified that the conclusions in the above Decision were reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

ERNESTO D. ACOSTA
Presiding Justice