LA TONDEÑA, INC.,
Petitioner,

versus CTA CASE NO. 1554

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

x - - - - - - - - - - x

Dec. 3/68

D E C I S I O N

This is an appeal from the decision of respondent dated October 19, 1964 (Exh. 8, pp. 54-55, BIR rec.) holding petitioner liable for the payment of ₱86,089.50 as specific tax on 123,000 proof liters of rectified alcohol allegedly lost through evaporation, aging, and handling.

Petitioner is a domestic corporation engaged in business as a rectifier, compounder of wines and liquors, denaturer of alcohol, and manufacturer of rubbing alcohol and lime juice. In the manufacture of its products, petitioner uses distilled spirits purchased from various sugar centrals, principally from Central Azucarera Don Pedro, Nasugbu, Batangas, and Central Azucarera de Tarlac, Tarlac, Tarlac, which are original distillers of alcohol. The alcohol purchased from the said sugar centrals were removed from their places of production to the rectifying plant of petitioner in Tondo, Manila, without prepayment of the specific tax because petitioner (rectifier of alcohol) and the sugar centrals (distillers) executed a joint bond, with the express permission and approval of the respondent, conditioned upon future payment by the petitioner of the specific tax due on the finished product (See Section 129 of the Tax Code).

The distilled spirits (alcohol) were placed by petitioner in tanks, wooden oak barrels for aging, others sold to other compounders, and the bulk were used in its own compounding of wines and liquors. Upon receipt of the distilled spirits at the rectifying plant of petitioner, they were recorded in the "A" Account of the BIR Official Register Book under the heading "Received From Other Distilleries." The credit to the "A" Account represents the transfer of the distilled spirits for rectification. From the "A" Account the alcohol were transferred to the "B" Account wherein removals were made representing sales of rectified alcohol to other compounders of liquors, while others were transferred to the "C" Account for petitioner's own purposes in compounding wines and liquors. Upon removal from the "B" Account, after rectification, the specific tax on the alcohol was paid by petitioner.

Verification of the BIR Official Register Book by Revenue Inspectors Ernesto de Guia and Jose Chico, Jr. and Senior Revenue Inspector Carlos Eloriaga showed that in 1962, two (2) stock takings were conducted on January 11 and July 5, 1962, wherein losses of alcohol were indicated in the "A" Account. The losses amounted to 68,445.3 gauge liters of alcohol equivalent to 127,719 proof liters. The said losses were ascertained to have been due to storage, evaporation, handling, or aging of already rectified alcohol while in tanks and wooden oak barrels, and itemized as follows:

Losses

Date	In Tanks		In Oak Barrels		Total	
	G.L.	P.L.	G.L.	P.L.	G.L.	P.L.
Jan. 19/62	22,674.5	45,018	3,696.3	4,796	26,360.8	49,814
July 5/62	39,447	74,794	2,637.5	3,111	42,084.5	77,905
T O T A L	62,121.5	119,812	6,333.8	7,907	68,445.3	127,719

On July 22, 1963, petitioner was assessed by respondent in the total amount of ₱90,786.77 for specific tax, advance sales tax, and privilege taxes and penalty, computed as follows:

1.	Specific tax	₱ 89,403.30
2.	Advance sales tax . . .	1,083.47
3.	Privilege taxes (B-18) including compromise penalty	300.00
	T O T A L	₱ 90,786.77

(Exh. 4, p. 30, BIR rec.)

After payment of items 2 and 3 (See photostat of Official Receipt No. C-1608836, dated August 15, 1963, p. 32, BIR rec., and Exhibits D & E, pp. 9-12, CTA Rec.) petitioner appealed the assessment of respondent to this Court and questioned the legality of the specific tax assessment of ₱89,-403.30 (less ₱3,313.80, paid) based on Section 129 of the National Internal Revenue Code, in relation to Section 133 of the same Code.

The issues submitted by the parties to the Court for resolution are the following:

> 1. Whether or not the distilled spirits purchased by petitioner from the sugar centrals were rectified alcohol; and
>
> 2. Whether or not alcohol losses through evaporation, aging, handling and/or rectification are subject to the specific tax imposed by Section 133 of the National Internal Revenue Code, in relation to Section 129 of the same Code.

First Issue -

Petitioner contends that the alcohol purchased by it from the sugar centrals were crude spirits requiring rectification and not rectified alcohol. This contention is bolstered solely by the testimony of petitioner's chemist, Mr. Miguel Posadas. He testified that the alcohol purchased by petitioner were lower in quality and less in proof compared with the standard United States alcohol. He pointed out that the standard of rectified alcohol is 60 minutes per manganate time test and above 189 proof as the grade of alcohol, that is, 190 proof or above is considered as rectified alcohol in the United States (p. 7, t.s.n.). He further testified that the alcohol purchased by petitioner from the sugar centrals were only 189 proof and, therefore, it contains impurities like acids, esters and fusel-oils which, in order to meet the standard set by petitioner in its business of manufacturing quality wines and liquors, must be removed through chemical process or physical means (pp. 7-10, 24-25, t.s.n.). In short, according to petitioner's witness, the alcohol purchased by it is only 189 proof.

Respondent contends, however, that the alcohol purchased by petitioner from the sugar centrals were not crude spirits but rectified alcohol. It is alleged that the said alcohol were used by petitioner in its principal business as a compounder of distilled spirits (manufacturer of wines and liquors) by utilizing rectified alcohol as its basic raw material. It is claimed that, while petitioner is only a rectifier and not a distiller, the sugar centrals from which the alcohol were purchased are well known and reputable original distillers or producers of quality alcohol. Moreover, in order to meet the high standard quality set by petitioner in the manufacture of its wines and liquors, the rectified alcohol already purchased were re-rectified and/or aged in wooden oak barrels. Respondent's contention finds support in the official report of his revenue inspectors, based upon an on the spot examination of petitioner's business operation (Exh. 2, pp. 15-18, BIR rec.) and on the 3rd indorsement, dated November 11, 1963, of the Head of the Alcohol Tax Unit of the Investigation Division, Bureau of Internal Revenue (Exh. 7, pp. 37-39, BIR rec.).

Respondent's view is well taken. The conclusion made by petitioner's witness that the alcohol purchased by it from the sugar centrals were only <u>189 proof</u> as grade of the alcohol, instead of 190 proof as provided in the Code of Federal Regulations (U. S.), does not justify petitioner's sweeping statement that the alcohol purchased from the sugar centrals were crude spirits (low test alcohol) and not rectified alcohol in the absence of convincing and satisfactory evidence to that effect. The mere fact that the alcohol purchased from the sugar centrals still contain certain minor impurities does not mean that the alcohol is crude even if further rectification or re-rectification thereof is pursued by the petitioner. After all, the re-rectification of the alcohol to remove a minor impurity is but a business policy of petitioner in order to meet the high standard demanded of its manufactured wines and liquors. A person need not be an expert or connoisseur of liquors to know that different kinds or brands of liquor have different degrees of proof, depending upon the standard set by the manufacturer.

Section 194 of the National Internal Revenue Code defines the distillers of spirits as follows:

> (b) "Distillers of spirits" comprises all who distill spirituous liquors <u>by original and continuous dis-</u>

> tillation from mash, wort, wash, sap, or syrup through continuous closed vessels and pipes until the manufacture thereof is complete. (Underscoring supplied)

The sugar centrals from which the alcohol in question were purchased are well known and reputable distillers of spirits. As such distillers, the alcohol produced by them were made by original and continuous distillation and, therefore, the said alcohol are considered by our law (not regulation) as rectified alcohol and not crude spirits, in line with Section 129 of the Tax Code which provides, among others, as follows:

> . . . And provided, further, That in cases where alcohol has already been rectified either by original and continuous distillation or by redistillation is further rerectified, no loss for rectification and handling shall be allowed and the rectifier thereof shall pay the specific tax due on such losses. (As amended by sec. 5, Republic Act No. 1608.) (Underscoring supplied)

It is very clear, therefore, from the definition of "distillers of spirits" found in Section 194(b) of the Tax Code, in relation to Section 129 of the same Code, supra, that rectified alcohol are produced by two (2) processes, namely: (1) by original and continuous distillation; and (2) by redistillation. Consequently, the alcohol sold by the sugar centrals (produced by original and continuous distillation) to the herein petitioner and recorded in the "A" Account of the BIR Official

Register Book are rectified alcohol and not crude spirits.)

Second Issue -

Petitioner's stand that it is not liable to the specific tax of ₱66,089.50 as well as to 1% loss through evaporation while the alcohol remained in storage is anchored in the decision of this Court in the case of Central Azucarera de Tarlac v. Commissioner of Internal Revenue, CTA Case No. 954, and Section 22 of Revenue Regulations No. 3, as amended by Section 3 of Revenue Regulations No. 24 of the Department of Finance, which provides as follows:

> Section 22. Losses and overages. - No tax will be refunded on distilled spirits lost or destroyed by accident after their removal from the distillery wherein produced, nor will the collection of the tax be waived on bonded spirits similarly lost or destroyed.
>
> The Internal revenue tax attaches to distilled spirits as soon as they come into existence as such, and any loss which occurs before removal of same must be accounted for in the official register book of the distillery. Losses in rectification of crude spirits and losses in compounding liquor will be ascertained by the gauger, verified by the internal revenue agent, and credited on the auxiliary register books as they occur. A loss not exceeding 7 per cent in rectification and 2 per cent in compounding may be allowed by the Collector of Internal Revenue when such a loss is not caused by fraud, negligence or carelessness of the distillers or owners of the rectifying establishments. Other losses exceeding 1 per cent of the total stock handled since the last stock taking will also be subject to disallowance.

Unfortunately, the foregoing provisions of the Revenue Regulations are no longer in force by virtue of the amendment of Section 129 of the Tax Code by Section 3 of Republic Act No. 1608, which took effect on August 23, 1956. The amendatory provisions read as follows:

> "SEC. 129. Removal of spirits or cigars under bond.—Spirits requiring rectification may be removed from the place of their manufacture to some other establishment for the purpose of rectification without the prepayment of the specific tax, provided the distiller removing such spirits and the rectifier receiving them shall file with the Collector of Internal Revenue their joint bond conditioned upon the future payment by the rectifier of the specific tax that may be due on any finished product; x x x And provided, further, That in cases where alcohol has already been rectified either by original and continuous distillation or by redistillation is further re-rectified, no loss for rectification and handling shall be allowed and the rectifier thereof shall pay the specific tax due on such losses."

The present case is on all fours with the previous case of the same parties entitled Collector of Internal Revenue v. La Tondeña, Inc., G.R. No. L-10431, decided by our Supreme Court on July 31, 1962, the pertinent portions of which read as follows:

> "SEC. 133. Specific tax on distilled spirits. - On distilled spirits there shall be collected, except as hereinafter provided, specific taxes as follows:
>
> x x x x x

> 'Distilled spirits', as here used, includes all substances known as ethyl alcohol, hydrated oxide of ethyl, or spirits of wine, which are commonly produced by the fermentation and subsequent distillation of grain, starch, molasses, or sugar, or of some syrup or sap, including all dilutions or mixtures; <u>and the tax shall attach to this substance as soon as it is in existence as such, whether it be subsequently separated as pure or impure spirits, or be immediately or at any subsequent time transformed into any other substance either in process of original production or by any subsequent process</u>.'

"Pursuant to the above provision of law, therefore, 'the tax shall attach to this substance as soon as it is in existence as such' etc. However, <u>on January 1, 1951</u>, Republic Act No. 592 took effect, amending section 133 and the clause underlined above had been eliminated. The evident intention of the lawmaker in deleting the all embracing underlined clause, was to subject to specific tax not all kinds of alcoholic substances, <u>but only distilled spirits as finished products</u>, actually removed from the factory or bonded warehouse. The said amendment could not mean anything else; it is in harmony with section 129, of the same Tax Code which provides -

> "SEC. 129. <u>Removal of spirits or cigar under bond</u>. - <u>Spirits requiring rectification</u> may be removed from the place of their manufacture to some other establishment for the purpose of rectification without the prepayment of the specific tax, provided the distiller removing such spirits and the rectifier receiving them shall file with the Collector of Internal Revenue their joint bond conditioned upon the future payment by the rectifier of the <u>specific tax that may be due on any finished product</u>. x x x.

And if one would consider that the Tax Code does not prohibit further rectification or distillation and defines in section 194 thereof, a rectifier as a person who rectifies, purifies or refines distilled spirits, the conclusion is logical that when alcohol, even if already distilled (as in the present case) or rectified, is again rectified, purified or refined, <u>the specific tax should be based on the finished product</u>, and not on the evaporated alcohol. The intention not to subject to specific tax all kinds of alcoholic substances but only distilled spirits as finished products, is reflected in former Senator Garcia's observations on the floor of the Senate, during the discussion of House Bill No. 1443 (now Rep. Act No. 592), when he proposed the elimination of the phrase "and the tax shall attach to this substance as soon as it is in existence as such, etc." He said -

xx xx xx xx xx

> "That is why, Mr. President, in Section 1 of this Bill now under consideration, <u>I have some serious objections to the provisions where all kinds of alcoholic substance</u> which falls under the definition of proof spirits in the last paragraph of the same Section 1 of the proposed measure <u>are taxable because this is one of those that I consider of deterrent effect to the industrialization of this country</u>. . . (Senate Diario No. 6, Jan. 15, 1951, Original, 4th Special Session; Italics supplied."

And on August 23, 1956, upon the recommendation of the Bureau of Internal Revenue itself, Rep. Act No. 1608 was passed, amending section 133 of the Tax Code, as amended by R. A. No. 592, restoring the very same clause which was eliminated (Sec. 7, R.A. No. 1608). The inference, therefore, is clear that from January 1, 1951, when Rep. Act No. 592 took effect, until August 23, 1956, when R.A. No. 1608 became a law, the tax on alcohol did not attach as soon as it was in existence as such, but on the finished product. And this must be so, otherwise a great injustice would be caused upon a duly licensed rectifier, who, like the respondent herein, will be made to pay the specific tax on the alcohol lost thru evaporation, from which no one has been benefited, based on the provision of laws then extant, of doubtful application. In every case of doubt, tax statutes are construed most strongly against the government and in favor of the citizens, because burdens are not to be imposed beyond what the statutes expressly and clearly import (MRR Co. v. Coll. of Customs, 52 Phil. 950; Luzon Stev. Co. v. Trinidad, 43 Phil. 803, 809). It should be pointed out also that said section 129 was amended by adding the following -

> "And provided, further, That in cases where alcohol has already been rectified either by original and continuous distillation or by redistillation is further rectified, no loss for rectification and handling shall be allowed and the rectifier thereof shall pay the specific tax due on such losses" (Sec. 5, Rep. Act No. 1608).

which obviously reveals that the purpose of the amendment is to tax, only now, alcohol lost, in further distillation or rectification. This law certainly should not be given a retroactive effect, so as to cover the period in question (January 1, 1951 to February 27, 1954). It is only after August 23, 1956 that the government woke up from its lethargy and hastened to fill the hiatus.

Petitioner contends that the doctrine enunciated by our Supreme Court in the above-entitled case is not applicable to the present case because the old case refers to losses in further distillation or rectification of alcohol and not to losses while the same remained in the storage tanks of petitioner. Suffice it to say that the evidence of petitioner on this point is inherently weak and self-serving. As admitted by petitioner's witness and as officially reported by the revenue inspectors of respondent, the bulk of the alcohol in question had been further rectified by petitioner in order to remove the impurities therein to meet the high standard demanded of petitioner's manufactured wines and liquors.

WHEREFORE, finding no error in the decision of respondent appealed from, the same is hereby affirmed and petitioner is, therefore, ordered to pay respondent or his duly authorized collection agent the sum of ₱86,089.50 as specific tax on rectified alcohol lost through evaporation and handling. With costs against petitioner.

SO ORDERED.

Quezon City, December 3, 1967.

Estanislao R. Alvarez
ESTANISLAO R. ALVAREZ
Associate Judge

WE CONCUR:

R M Umali
ROMAN M. UMALI
Presiding Judge

Ramon L Avanceña
RAMON L. AVANCEÑA
Associate Judge