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REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
MANILA

CENTRAL AZUCARERA DON PEDRO,
Petitioner,

- versus - C.T.A. CASE NO. 387

THE COLLECTOR OF INTERNAL REVENUE,
Respondent.

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Feb. 24/58

D E C I S I O N

This is an appeal from the decision of the Collector of Internal Revenue assessing against, and demanding from, the petitioner Central Azucarera Don Pedro, specific tax on denatured alcohol in the amount of ₱33,696.60, and compromise penalty of ₱10,000.00 for alleged violation of sections 124 and 133 in relation to section 127, all of the National Internal Revenue Code.

The petitioner herein, Central Azucarera Don Pedro, is a domestic corporation duly established and organized under the laws of the Philippines, with a principal place of business at Nasugbu, Batangas. Among other things, it is authorized to operate a duly registered distillery plant. Between the period from March 23, 1953, to August 13, 1954, the petitioner manufactured in its distillery, 284,423 proof liters of denatured alcohol under a special formula admitted by both parties in their pleadings to be as follows:

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> "To every 100 gauge liters of rectified Alcohol of not less than 180 degrees proof, there shall be added 10 liters of Isopropyl."

This denatured alcohol was sold by the petitioner to the Pacific Products, Inc. and the Pacific Industrial Manufacturing, who in turn used it in the manufacture of rubbing alcohol compound and other products containing specially denatured alcohol as ingredient. The rubbing alcohol compound produced by the two last mentioned buyers contains 70% alcohol and, as appearing on the labels pasted to the containers, Exhibits 1 and 2, is intended for use as "disinfectant, sterilization, sanitation, bathing, massage, rubbing or other external uses."

The preparation, sale, and withdrawal of this denatured alcohol sold to the two buyers was admittedly with the permission and authority of the respondent through his Denaturing Committee and at the time of the sale and withdrawal the said committee never made any demand from the petitioner for the payment of the specific tax in question. However, petitioner paid the corresponding sales tax on the denatured alcohol sold to the two buyers.

As heretofore stated, the denaturization was done in accordance with a formula approved by the respondent. The process of denaturization, as evidenced by Exhibits A to A-25, was witnessed by a Denaturing Committee consisting of three members, all representatives of the respondent. After the process of denaturization, but during that same day, the said committee accomplished denaturization certificates, Exhibits A to A-25, attesting to the chief ingredients used, the denaturing agent mixed and the amount of proof liters produced as well as the percentage of their alcoholic contents. The resulting denatured alcohol was correspondingly recorded in an Official Register Book, Exhibits B to B-9 under BIR Form No. 2.41, by the owner or manager of the corporation and attested to by an Internal Revenue agent. The denaturization certificates, Exhibits A to A-25, show therein that the denatured alcohol was exempted from payment of specific tax by the Denaturing Committee.

On the basis of a report, Exhibit 3 (pp. 3-4 BIR rec.), dated May 26, 1955, of Revenue Agents Mariano P. Uy and Venancio V. Ona, the respondent wrote a letter, Exhibit 4 (pp. 11-12 BIR rec.) dated May 30, 1955 assessing and demanding from the petitioner the sums of ₱199,906.10 as specific tax on the said 284,423 proof liters of denatured alcohol and ₱10,000.00 as compromise penalty.

After a reinvestigation and finding that out of the total of 284,423 proof liters of denatured alcohol removed from petitioner's distillery, only 48,138 proof liters were actually used by the Pacific Industrial Manufacturing and the Pacific Products, Inc. in the production and manufacture of rubbing alcohol compound, the respondent, on May 24, 1957, wrote a letter, Exhibit E (p. 44 BIR rec.) notifying the petitioner through counsel that the original assessment and demand for specific tax against it was reduced from ₱199,906.10 to ₱33,696.60 exclusive of the compromise penalty of ₱10,000.00. It appears by agreement of the parties that the rest of the denatured alcohol amounting to 236,285 proof liters after deducting the amount used in the manufacture of rubbing alcohol, was utilized by the two buyer-corporations in the manufacture of shellac, varnish, lacquer thinner, wood dye, glass cleanser and cleaning fluids.

The main issue raised by the parties in this appeal is whether or not the 48,138 proof liters of denatured alcohol sold by the petitioner to the Pacific Products Inc. and the Pacific Industrial Manufacturing and used by the latter as raw materials in the manufacture and production of rubbing alcohol compound should be subjected to the payment of specific tax pursuant to Section 124 in relation to Sections 127 and 133 of the National Internal Revenue Code.

The pertinent sections of the National Internal Revenue Code upon which respondent's assessment and demand is based are reproduced hereunder:

> "Sec. 124. Payment of Specific Tax on domestic products.- Specific taxes on domestic products shall be paid by the manufacturer, producer, owner, or person having possession of the same; and, except as otherwise specially allowed, such taxes shall be paid immediately before removal from the place of production."

> "Sec. 127. Tax on preparations containing distilled spirits as chief ingredient.-- Medicinal and toilet preparations,

> flavoring extracts, and all other preparations, of which, excluding water, distilled spirits form the chief ingredient, shall be subject to the same tax as such chief ingredient."
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> "Sec. 133. Specific tax on distilled spirits.--On distilled spirits there shall be collected subject to the provisions of section one hundred and twenty-eight of this Act, except as hereinafter provided, specific taxes as follows:
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> "(a) If produced from sap of nipa, coconut, cassava, camote, or buri palm, or from the juice, syrup, or sugar of the cane, per proof liter, seventy centavos;
>
> x x x x
>
> "'Distilled spirits', as here used, include all substances known as ethyl alcohol, hydrated oxide of ethyl, or spirits of wines, 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."

Petitioner contends that the denatured alcohol which was removed from its distillery by the two buyers and used by the latter in the production and manufacture of rubbing alcohol compound are not "medicinal preparations" subject to specific tax under section 127 of the Tax Code, in relation to section 133 of the same Code. Petitioner argues that "Even if it were hypothetically assumed that rubbing alcohol, x x x, is a medicinal preparation, it is not subject to specific tax under section 127" because this section subjects to specific tax only those articles mentioned therein the chief ingredient of which is capable of oral intake or internal consumption.

We cannot sustain the contention of the petitioner.

It was proven by the testimony of Dr. Benjamin Buensuceso, a resident physician of the Philippine General Hospital, that denatured alcohol is a medicinal preparation. Besides, we have had occasion to hold in a case involving this same question that denatured alcohol, which was made the chief ingredient of rubbing alcohol compound, is a medicinal preparation. (See La Tondeña, Inc. vs. Collector of Internal Revenue, C.T.A. Case No. 182, December 16, 1957.) The fact that the medicinal preparations are not capable of oral intake or internal consumption is of no importance for the purpose of imposing specific taxes thereon. The law is general and speaks of "medicinal and toilet preparations" and "all other preparations" of which distilled spirit is the chief ingredient. It does not make any distinction whether these products are potable or not. (La Tondeña, Inc. vs. Collector, Ibid.)

The petitioner further contends that the denatured alcohol produced and sold to the two corporations are exempt from specific tax under section 128 of the Internal Revenue Code, which provides:

> "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 of the distiller or of the Government 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 and industries. (Underlining supplied.)

Although it was proven by petitioner that the two corporations to which it sold the denatured alcohol were engaged in an industry - the manufacture of chemical products - and utilizing a seizable amount of labor and capital (pp. 42-44, t.s.n.) yet, as we had previously held in the La Tondeña case, supra, in order that the denatured alcohol in question could be exempted under the provision of the Tax Code just quoted above it must be so used for the operation of such industries and not merely as an ingredient in the manufacture of another product.

Granting that the rubbing alcohol compound in controversy is subject to specific tax, the petitioner maintains that it is not liable for the payment of the same. Petitioner argues that under Section 124 of the National Internal Revenue Code "specific taxes on domestic products shall be paid by the manufacturer, producer, owner or person having possession of the same x x x before removal from the place of production." Inasmuch as the rubbing alcohol compound is not a product of the petitioner but of Pacific Products, Inc., and Pacific Industrial Manufacturing, the petitioner concludes that the said two corporations should be made to pay the specific tax on the rubbing alcohol.

We find this last alternative contention of the petitioner to be meritorious. It is true that the denatured alcohol which forms the chief ingredient of the rubbing alcohol compound, was manufactured by the petitioner. However, the denatured alcohol was never re- 11 moved by the petitioner from its distillery with the intention of evading the payment of the specific taxes thereon. On the contrary, the same was sold by the petitioner to Pacific Products, Inc., and Pacific Industrial Manufacturing, and when the said two corporations assumed control and possession of the denatured alcohol, they acquired the ownership over the same. (Arts. 1477 and 1497, Civil Code of the Philippines). Subsequently, with the permission and the authority of the respondent, they removed the denatured alcohol from petitioner's distillery, and with it as the principal raw material, they manufactured the rubbing alcohol compound on which the respondent assessed and now seeks to collect the disputed specific tax. To our mind, it is clear that Pacific Products, Inc., and Pacific Industrial Manufacturing, are the manufacturers, producers, and/or owners of the rubbing alcohol compound, and considering that the law (Sec. 124, National Internal Revenue Code) does not require the specific tax to be paid immediately before the sale (Benito Garcia vs. The Collector of Internal Revenue, 66 Phil. 441), we are of the opinion and so hold that the said corporations who purchased the denatured alcohol from the petitioner, are liable for the payment of the specific tax in question, and not the petitioner herein.

WHEREFORE, the decision of respondent appealed from, should be, as it is hereby reversed. Petitioner

Central Azucarera Don Pedro is hereby declared not liable for the payment of the sum of ₱33,696.60 representing specific tax assessed by the respondent, without prejudice to whatever action the respondent may decide to take against the proper party or parties liable therefor. Without pronouncement as to costs.

SO ORDERED.

Manila, February 28, 1958.

AUGUSTO M. LUCIANO
Associate Judge

WE CONCUR:

MARIANO NABLE
Presiding Judge

I concur in the result solely on the grounds stated in my dissenting opinion in La Tondeña, Inc. v. Collector of Internal Revenue, C.T.A. No. 182, Dec. 16, 1957.

ROMAN M. UMALI
Associate Judge

Affd. in G.R. No. L-14015, May 31, 1960.