REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
MANILA

LA TONDEÑA, INC.,
Petitioner,

- versus -

C.T.A. CASE NO. 182

COLLECTOR OF INTERNAL REVENUE,
Respondent.

Dec. 16, 1957

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D E C I S I O N

This is an appeal from the decision of the respondent Collector of Internal Revenue assessing and demanding from the petitioner, La Tondeña, Inc., the payment of the sum of ₱268,153.73 as specific tax on 391,396 proof liters of denatured alcohol produced by it during the period from July, 1951 to May, 1954, inclusive, plus a penalty in the amount of ₱10,000.00 for alleged illegal removal of alcohol from the place of production without prepayment of the specific tax due thereon in violation of Section 124 in relation to Sections 127 and 133, and penalized under Section 174 all of the National Internal Revenue Code.

The petitioner, La Tondeña, Inc. is a corporation duly organized and existing under the laws of the Philippines. Aside from the manufacture of wines and liquors, the petitioner is also a duly licensed rectifier of alcohol which is removed from the place of original distillation without prepayment of the specific tax but under bond approved by the respondent conditioned upon petitioner's payment of the specific tax that may be due on the finished product, as provided for in Section 129 of the Tax Code. It is also engaged in denaturing ethyl alcohol for the manufacture of rubbing alcohol either for its own use or for sale to the public under the brand "Jai Alai" rubbing alcohol or for the use of the different grantees of special formulas, approved by the Bureau of Internal Revenue, for the manufacture of fuel, shellac, rubbing alcohol and other products specified in the grantee's permit.

In denaturing alcohol, the petitioner uses three formulas, namely: (1) Under the general formula using methyl alcohol and pyridine bases as ingredients which composition is used for fuel or light; (2) under the special formula using castor oil, or methanol and uranin solution, or some other ingredients which composition is used for the manufacture of shellac, wood dye, or for some other industrial purposes; and (3) under the special formulas enumerated in the report (pp. 1-18, BIR rec.) of Agents Mariano P. Uy and Venancio Ona all of which are authorized by the Bureau of Internal Revenue.

Before denaturing the alcohol for each general or special formula, the petitioner if for its own use, or the different grantees if for their own use, secures first the approval of the Collector of Internal Revenue. Thereafter, a date is fixed for the denaturing of the alcohol, and at the place and on the date and hour fixed, a denaturing committee composed of members appointed by the Collector, from three (3) to five (5) in number, witness the pouring of the ingredients specified in the approved formula to the alcohol, and the resulting compound is then packed in containers or drums which are painted and lettered with the information as specified by the Bureau of Internal Revenue, different in color from the drums used for tax paid alcohol.

The subject matter of the present assessment and demand are the denatured alcohol used by the petitioner in the manufacture of its "Jai Alai" rubbing alcohol and the alcohol specially denatured by the petitioner and sold to different purchasers. All the ethyl alcohol used in the denaturing were 189° proof, and all the alcohol denatured were entered by the petitioner and attested by the representative of the Bureau of Internal Revenue in the Official Register Book known as Account D-1, which is a book wherein only denatured alcohol are recorded.

On June 24, 1954, Internal Revenue Agents Mariano P. Uy and Venancio V. Ona reported, after due investigation, that from July, 1951 to May, 1954, the petitioner did not pay the specific tax on 391,396 proof liters of ethyl alcohol which were denatured and used in the preparation of rubbing alcohol and other medicinal preparations, but instead, it paid the 7% sales tax on the sale of the said preparations. The specific tax due thereon was ascertained and computed to be ₱273,977.20, but inasmuch as the petitioner has already paid the sum of ₱5,823.47 as sales tax, the respondent, on July 26, 1954, issued an assessment and demand for the payment of the sum of ₱268,153.73 as specific tax on said alcohol, plus the amount of ₱10,000.00 as penalty, which assessment and demand is now under review.

The only question to be decided in this appeal is whether or not the petitioner is subject to the specific tax prescribed in Section 127 in relation to Section 133, both of the National Internal Revenue Code, on its "Jai Alai" rubbing alcohol and the specially denatured alcohol which it produced and manufactured in accordance with special formulas for its different customers.

The pertinent provisions of Sections 127 and 133 of the Tax Code provide as follows:

> "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." (Underscoring supplied.)

> "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:

> "(a) If produced from sap of the nipa, coconut, cassava, camote, or buri palm, or from the juice, syrup, or sugar of the cane, per proof liter, seventy centavos;

> "(b) If produced from any other materials, per proof liter, ten pesos.

> "This tax shall be proportionally increased for any strength of the spirits taxed over proof spirits."

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On the authority of the provisions of law quoted above,,the respondent Collector of Internal Revenue assessed and demanded from the petitioner the deficiency specific tax in question. The respondent contends that the specially denatured alcohol manufactured and produced by the petitioner herein, some of which were used by it in the manufacture of its "Jai Alai" rubbing alcohol and the rest sold to the different grantees given permits by the Bureau of Internal Revenue, are medicinal preparations, the chief ingredient of which is distilled spirits, and hence subject to the specific tax on distilled spirits.

The first inquiry therefore turns upon the meaning of the terms "medicinal preparations" and "toilet preparations". The following definitions are in point:

> "'Medicinal preparation'- the term has the same meaning in trade and commerce as in common speech and is descriptive of and refers to substance used in medicine and prepared for the use of the apothecary or physician to be adminitered as a remedy in disease." (Law Dictionary with Pronounciation, Ballantine, Philippine Edition."
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> "The expression 'medicinal preparation' as used in Tariff Act March 3, 1883, C. 121, Schedule A, 22 Stat. 494, means such articles as are of use or believed by the prescriber or user fairly and honestly to be of use, in curing or alleviating or palliating or preventing some disease of affection of the human frame." (Words & Phrases, Vol. 26A, p. 617.)
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> "'Medicinal' means curative or alleviative; used for the cure or alleviation of body disorders." (Words & Phrases, Vol. 26A, p. 616.)

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> "'Toilet water' - a perfumed liquid, usually weakly alcoholic, as cologne or Florida water, used in or after a bath, or as a freshner of the skin." (Webster's New International Dictionary.)

> "'Preparation' is that which is prepared, or something equipped or compounded for a partcular purpose." (Words & Phrases, Vol. 33, p. 380.)

Mr. Rectorino B. Cruz, Pharmacist of the Reme Pharmaceutical Laboratory, testified to the effect that denatured alcohol could be considered as medicinal preparation because it can be used as an antiseptic and inhibits the growth of bacteria (pp. 120-121, 135-138 t.s.n.). This view is shared by Mrs. Clemencia de Dios, Chief Pharmacist of the Quezon Institute (pp. 215-219 t.s.n.); by Dr. German Castillo, Resident Physician of the Philippine General Hospital (pp. 397-406 t.s.n.); by Dra. Basilia-Zialcita Taningco, Pharmacist of the Philippine General Hospital (pp. 151-153 t.s.n.); and by Angel Arambulo, Pharmacist and Instructor of the College of Pharmacy, University of the Philippines. (tsn p.178-180.)

In the light of the literal meaning of the term "medicinal preparation," and the opinion of experts as stated above and considering that the Drug and Cosmetic Regulations has classified and considered alcohol as medicine (see 43 O.G. No. 2, Feb. 1947, pp. 406-419), we hold therefore that the specially denatured alcohol manufactured and produced by the petitioner is a <u>medicinal preparation</u>.

We shall now procded to determine whether or not distilled spirits is the chief ingredient of the dena-

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tured ethyl alcohol in question. Distilled spirits as defined in Section 133 of the Tax Code 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." (Underscoring supplied.)

Thus, under this definition, ethyl alcohol is considered distilled spirits. Considering this statutory definition and General Circular No. 468 of the Bureau of Internal Revenue, dated September 18, 1940, which states in part that "alcohol shall be considered the chief ingredient of medicinal preparations if after excluding water, alcohol constitutes more than 50% of the preparation by volume," we are of the opinion and so hold that the specially denatured alcohol prepared and produced by the petitioner herein, some of which were used by it in the manufacture of its "Jai Alai" rubbing alcohol and the rest sold to its customers who used the same as rubbing alcohol and for medical and surgical purposes, is subject to the specific tax prescribed by Section 127 in relation to Section 133 of the Tax Code. A cursory perusal of the different formulas used by the petitioner, in making the specially denatured alcohol supports this conclusion. All these formulas show that ethyl alcohol which by express provision of law is classified as "distilled spirits" is the chief ingredient of said preparations.

However, the petitioner contends that for a preparation the chief ingredient of which is distilled

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spirits to be subject to specific tax, the same must be potable or capable of being taken internally. It argues that since the denaturants used rendered the alcohol unfit for internal consumption, it follows that the specially denatured alcohol cannot be considered as distilled spirits taxable under Section 127 in relation to Section 133 of the Tax Code.

We are of the opinion that such an interpretation is erroneous and farfetched. The law is general and speaks of "medicinal and toilet preparations" and "all other preparations" of which distilled spirits is the chief ingredient. It does not make any distinction but subjects such preparations alike to the specific tax. Ubi lex non distinguit, nec nos distinguere debemus.

Moreover, in the imposition of the specific tax on alcohol as a medicinal preparation, the circumstance of whether it is capable of oral intake or internal consumption is not taken into account. It is sufficient that alcohol has been manufactured and produced, and the specific tax thereon immediately attaches. (Sec. 124, N.I.R.C.)

The petitioner also maintains that the alcohol in question was used for industries and is therefore exempt from specific tax under Section 128 of the Tax Code which reads as follows:

> "Sec. 128. Exemption in favor of domestic denatured alcohol.- Domestic alcohol of not less than one hundred eighty degrees

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> 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 payment 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."

We find petitioner's contention untenable and without merit, and on the contrary, we believe that the exemption under Section 128 of the Tax Code refers to domestic denatured alcohol used in the operation of industries and not to denatured alcohol to be used merely as an ingredient in the manufacture of another product. To hold otherwise would render nugatory and without effect Section 127 of the Tax Code for it is undeniable that the manufacture of medicinal, toilet and other preparations are industries. Congress in enacting Sections 127 and 128 could not have intended to impose a tax in one section, only to exempt in the following section. It is a cardinal rule of interpretation that provisions of law should be interpreted in such a manner as to harmonize the same with other provisions. Moreover, exemptions from taxation are highly disfavored in law and must be strictly construed. He who claims exemption must be able to justify his claim by the clearest grant of organic or statute law. (Collector vs. Manila Jockey Club, Inc., 53 O.G. 3762; Panay Electric Co. vs. Collector, G. R. No. L-6753, July 30, 1955.)

How about th[illegible] exempted in certain agriculture for reasons used in other industries

The petitioner further argues that the new interpretation given by the respondent to Sections 127 and

128 of the Tax Code should not be given a retroactive effect. It claims that for the last twenty (20) years it had been relying on the previous rulings and permits of the Bureau of Internal Revenue, and consequently, it did not take into consideration the amount of specific tax in its sale of the specially denatured alcohol to the different grantees of permits and in its sale of its "Jai Alai" rubbing alcohol to the consuming public.

This question of whether or not an administrative officer is bound by the previous rulings of his predecessors in office has already been squarely decided by the Supreme Court in the case of Hilado vs. Collector of Internal Revenue and The Court of Tax Appeals (53 O.G. 2481). Hence, it shall suffice to quote from said decision the applicable ruling of the Supreme Court in order to dispose of the present contention of the petitioner:

> "It cannot be denied, however, that the Secretary of Finance is vested with authority to revoke, repeal or abrogate the acts or previous rulings of his predecessors in office because the construction of a statute by those administering it is not binding on their successors if thereafter the latter becomes satisfied that a different construction should be given. (Association of Clerical Employees v. Brotherhood of Railway & Steamship Clerks, 85 F. (2d) 152, 109 A.L.R., 345.)
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> 'When the Commissioner determined in 1937 that the petitioner was not exempt and never had been, it was his duty to determine, assess and collect the tax due for all years not barred by the statutes of limitation. The conclusion reached and announced by his predecessor in 1924 was not binding upon him. It did not exempt the petitioner from tax.

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> This same point was decided in this way in Stanford University Bookstore, 29 B.T.A., 1280; affd., 83 Fed. (2d) 710.'" (Southern Maryland Agricultural Fair Association v. Commissioner of Internal Revenue, 40 B.T.A., 549, 554.)

And as to the retroactive effect that may be given to a new interpretation or construction of a tax law, the Supreme Court in the same case said:

> "With regard to the contention that General Circular No. V-139 cannot be given retroactive effect because that would affect and obliterate the vested right acquired by petitioner under the previous circular, suffice it to say that General Circular No. V-123, having been issued on a wrong construction of the law, cannot give rise to a vested right that can be invoked by a taxpayer. The reason is obvious: a vested right cannot spring from a wrong interpretation. This is too clear to require elaboration."

Moreover, the previous interpretation of Sections 127 and 128 of the Tax Code having been determined to be erroneous becomes a nullity. And as between the taxpayer and the Government, the taxpayer cannot plead the void act of an official to shield him from the demand of the Government that he pay the lawful specific tax that is demandable and due from him. The Government can neither be estopped nor prejudiced by the illegal acts of its servants. (Government v. Galarosa, 36 Phil. 338, 347.)

WHEREFORE, in view of the foregoing considerations, the decision of the respondent Collector of Internal Revenue assessing against and demanding from the petitioner La Tondeña, Inc., the payment of the sum of ₱268,153.73 as specific tax on the denatured alcohol it produced

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during the period from July, 1951 to May, 1954, inclusive, is hereby affirmed, and the petitioner is hereby ordered to pay the said amount to the respondent.

However, with respect to the imposition of the penalty in the sum of ₱10,000.00, the same being purely penal in nature, this Court has no jurisdiction over the same. (Ollada vs. Court of Tax Appeals, et al., 52 O.G. 4667.) With costs against the petitioner.

SO ORDERED.

Manila, Philippines, December 16, 1957.

AUGUSTO M. LUCIANO
Associate Judge

I CONCUR:

MARIANO NABLE
Presiding Judge

ROMAN M. UMALI
Associate Judge
dissents in a separate opinion.

(Note: Decision appealed in G.R. No. L-14336, not yet decided.)

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DISSENTING OPINION

I dissent. I cannot subscribe to the view that rubbing alcohol, a medicinal preparation manufactured out of denatured alcohol, is taxable at the same rates as alcoholic drinks. Because of the limitation imposed upon this Court by Section 13 of Republic Act No. 1125, I am unable to write a more extended opinion, but I shall do so at the proper time. For the present, I shall explain briefly three salient points in support of my view.

The first point I should like to emphasize is the wording of the law itself. Section 133 of the Revenue Code imposes a specific tax on distilled spirits, the amount of the tax depending upon the kind of materials used in the manufacture thereof. Section 127 imposes the same tax provided in Section 133 on medicinal preparations, flavoring extracts, and all other preparations, except toilet preparations, of which, excluding water, distilled spirits form the chief ingredient. And Section 128 exempts from the specific tax prescribed in Section 133 domestic alcohol of not less than one hundred eighty degrees proof when such alcohol is denatured and removed from the distillery or bonded warehouse for the purpose of being used for fuel, or light, or for use generally in the arts and industries. Section 3 of Republic Act No. 1608 has broadened the exemption so as to include denatured alcohol for use in hospitals, sanitaria, 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.

A careful analysis of Sections 127, 128 and 133 will readily show that the law classifies alcohol and alcoholic products into three categories, viz:

1. Distilled spirits, referring to alcoholic drinks, other than wines and fermented liquors which are taxable under Sections 134 and 135;

2. Medicinal preparations, flavoring extracts, and all other preparations, except toilet preparations, containing distilled spirits; and

3. Denatured alcohol for use as fuel or light, or for use generally in the arts and industries.[1]

The first class, referring to distilled spirits, is taxable under Section 133. Distilled spirits under this class are those intended for alcoholic beverages.

The second class, governed by Section 127, is of three kinds: (a) medicinal preparations, flavoring extracts, and all other preparations, of which, excluding water, distilled spirits form the chief ingredient;

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[1] The amendment introduced by Sec. 3, Rep. Act No. 1608, is not pertinent as the assessment here involved covers a period before the amendment.

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(b) preparations of which distilled spirits is not the chief ingredient; and (c) toilet preparations. Medicinal preparations, flavoring extracts, and all other preparations, of which, excluding water, distilled spirits form the chief ingredient, are taxable at the same rates as distilled spirits under Section 133. If the same articles do not contain distilled spirits as the chief ingredient, they are subject to the sales tax of 7% under Section 186. Toilet preparations, irrespective of alcohol content, are subject to the sales tax of 50% under Section 184.

The third class, referring to denatured alcohol for use as fuel or light, or for use generally in the arts and industries, are taxable under Section 142 (alcohol for motive power) and Section 186 (denatured alcohol used for light or in the arts and industries).

We are here concerned solely with the taxability of rubbing alcohol, admittedly a medicinal preparation manufactured by petitioner out of denatured alcohol. It is the contention of respondent that rubbing alcohol, being a medicinal preparation of which distilled spiaits is the chief ingredient, is taxable under Section 133 in relation to Section 127. On the other hand, petitioner claims that it is taxable under Section 186 in relation to Section 128.

I agree with petitioner that rubbing alcohol manufactured out of denatured alcohol is taxable under Section 186. In order that rubbing alcohol, as a medicinal preparation, may be subject to tax under Section 133 in relation to Section 127, it is essential that

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the alcohol used be distilled spirits and not denatured alcohol. Note that Section 127 uses the term "distilled spirits", as distinguished from the term "denatured alcohol" used in Section 128. Since the law has separately classified articles containing distilled spirits as the chief ingredient from denatured alcohol used generally in industries, and imposes different rates of taxes on each class, that classification must be respected.

It is contended that as a medicinal preparation rubbing alcohol is expressly classified in Section 127 and not in Section 128. This interpretation overlooks the essential requirement that a medicinal preparation must contain distilled spirits as the chief ingredient in order to be taxable under Section 133. If it was the intention of the legislature to tax all medicinal preparations containing alcohol, whether denatured or not, as the chief ingredient, it should have so expressly provided in Section 127. On the other hand, although Section 128 does not mention expressly the term "medicinal preparations" it makes mention of denatured alcohol used in industry. It cannot be denied that the manufacture of rubbing alcohol is an industry. Therefore, denatured alcohol used in the manufacture of rubbing alcohol is denatured alcohol used in industry and is taxable under Section 186 in relation to Section 128.

There is a valid reason for the distinction made by law between articles containing distilled spirits as the chief ingredient and articles manufactured out

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of denatured alcohol. And this is the second point to which I referred earlier in this opinion. The law imposing specific tax on distilled spirits or alcoholic beverages is both for revenue and for regulation, more for revenue. Medicinal preparations containing distilled spirits, not denatured, as chief ingredient must have to be taxed at the same rates as distilled spirits intended for beverages to prevent evasion of the high rates of tax on such articles. Medicinal preparations containing distilled spirits as chief ingredient could be used as substitute for alcoholic beverages. The same cannot be said of medicinal preparations manufactured out of denatured alcohol. They are poisonous. It is not possible to convert denatured alcohol into alcoholic beverages to evade payment of the corresponding specific tax considering the rigid regulations governing denaturing, which is actually done by a committee created by the Collector of Internal Revenue and composed of men mainly coming from the Bureau of Internal Revenue. The conversion could probably be done, but considering the high cost it would be cheaper to pay the specific tax. There is, therefore, no valid reason for placing medicinal preparations on the same level, for tax purposes, as distilled spirits intended for alcoholic beverages.

Could it have been the intention of the legislature to impose the same high rates of specific tax on medicinal preparations containing denatured alcohol as on distilled spirits for alcoholic beverages? Surely, the legislature could not have intended to regulate

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traffic in medicinal preparations which can not be used as a substitute for intoxicating beverages in the same manner that it has always sought to regulate traffic in intoxicating beverages.

Finally, I might also mention the fact that the exemption from specific tax of medicinal preparations manufactured out of denatured alcohol, and the taxation thereof under the sales tax provisions, has been the consistent practice of the Bureau of Internal Revenue for about half a century, if I am not mistaken, and was interrupted only sometime in 1954 when the present assessment was slapped against herein petitioner. A practice consistently followed and adhered to religiously for such a long period cannot be lightly disregarded. It is reasonable to suppose that a long standing practice of an executive department, if contrary to the intention of the legislature, would be specifically corrected by the legislative department. (1 USTC, Par. 259; see also 1 USTC, Par. 293.) Congress sought to correct what it considered an erroneous interpretation of the Collector of Internal Revenue in holding that vessels were subject to the sales tax or compensating tax by enacting Republic Act No. 361; it also enacted Republic Acts Nos. 894 and 1612 purportedly to correct an erroneous ruling that articles shipped abroad where title to the articles passed to the foreign buyers within Philippine jurisdiction were subject to the sales tax; and it also sought to correct a supposed erroneous interpretation in regard to the taxability of cement by enacting Republic Act No. 1299. These circumstances indicate that if Congress is dissatisfied with a standing practice, it enacts legislation to correct it. The fact that Congress has not amended the law relating to denatured alcohol as interpreted and administered by the Bureau of Internal Revenue for half a century gives rise to a strong presumption that the practice has received congressional approval.

FOR THE FOREGOING CONSIDERATIONS, it is my opinion that both the letter and the spirit of the law argue most strongly against the position taken by respondent, and, therefore, the decision appealed from should be reversed.

R. M. Umali

ROMAN M. UMALI
Associate Judge