REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

LA SUERTE CIGAR AND CIGARETTE FACTORY, INC.,
Petitioner,

- versus -

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

C.T.A. CASE NO. 5422

Promulgated:
JUN 11 1998

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DECISION

This case involves a claim for refund of Two Hundred Seventy Four Thousand Seven Hundred Thirty Eight Pesos and Fifty Centavos (₱274,738.50) representing specific taxes alleged to be erroneously collected from the petitioner during the month of September, 1994.

Petitioner, La Suerte Cigar and Cigarette Factory, Inc. (La Suerte, for brevity), is a domestic corporation engaged in the manufacture of cigars and cigarettes out of the stemmed leaf tobacco which it purchases in bulk from both local and foreign tobacco manufacturers.

On several occasions during the month of September of 1994, the Commissioner of Internal Revenue collected from La Suerte the aggregate amount of ₱274,738.50 for specific taxes allegedly due on La Suerte's bulk purchases of stemmed leaf tobacco from foreign tobacco

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manufacturers. La Suerte paid the said amount under protest.

On January 31, 1995, La Suerte, through counsel, filed a claim for refund of specific taxes which it paid on its importations of stemmed leaf tobacco covering the period from March 5, 1993 to September 16, 1994 in the aggregate amount of ₱4,684,018.50. This amount included the ₱274,738.50 subject matter of this petition.

By virtue of the inaction on the part of the Commissioner, La Suerte filed the instant petition on August 30, 1996.

The focal issue in this case is whether or not petitioner is entitled to the refund of the specific taxes covering the month of September, 1994.

Petitioner presented the following documentary evidence, to wit: letter claim for refund; Authority to Release Imported Goods dated August 31, 1989; Authority to Release Imported Goods dated September 12, 1994 and BIR Ruling dated December 12, 1972. Respondent's counsel waived the presentation of evidence but instead submitted the case for decision considering that the BIR records could not be located and that the case involves pure questions of law (TSN, 1-27-98).

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It is worthwhile to note that the parties stipulated on certain facts: the fact of filing of the claim for refund; unfavorable action on the part of the Commissioner; the stemmed leaf tobacco subject matter of the case were purchased from suppliers abroad which partially manufactured the same and the existence of two Authority to Release Imported Goods and BIR Ruling.

Accordingly, the above facts thus being settled, We now deal with the questions of law involved.

Petitioner relied on the provision of Section 137 of the National Internal Revenue Code (NIRC), which We quote:

> "**Section 137.** - ***Removal of tobacco products without prepayment of tax.*** - Products of tobacco entirely unfit for chewing or smoking may be removed free of tax for agricultural or industrial use, under such conditions as may by prescribed in the regulations of the Department of Finance. Stemmed leaf tobacco, fine cut shorts, the refuse of fine-cut chewing tobacco, scraps, cuttings, clippings, stems or midribs, and sweepings of tobacco may be sold in bulk as raw material by one manufacturer directly to another, without payment of the tax under such conditions as may be prescribed in the regulations of the Department of Finance. (Underscoring supplied).
>
> "Stemmed leaf tobacco" as herein used means leaf tobacco which has had the stem or midrib removed. The term does not include broken leaf tobacco."

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It is the position of petitioner that the aforecited law refers to all manufacturers of tobacco products because it does not mention any qualification. And as stipulated by both parties, the foreign suppliers of the subject stemmed leaf tobacco were also manufacturers of the same.

Respondent, for her part, does not believe that Section 137 of the Tax Code is the applicable law. She asserts that the governing law is Section 141 of the Tax Code which is reproduced below:

> "**Section 141.** ***Tobacco products.*** - There shall be collected a tax of seventy-five centavos on each kilogram of the following products of tobacco:
>
> (a) x x x
>
> (b) Tobacco prepared or partially prepared with or without the use of any machine or instruments or without being pressed or sweetened; and
>
> xxx xxx xxx
>
> Fine cut shorts and refuse, scraps, clippings, cuttings, stems and sweepings of tobacco resulting from the handling or stripping of whole leaf tobacco may be transferred, disposed of, or otherwise sold, without prepayment of the specific tax herein provided for under conditions as maybe prescribed in the regulations promulgated by the Secretary of Finance upon recommendation of the Commissioner if the same are to be exported or to be used in the manufacture of other

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> tobacco products on which the excise tax will eventually be paid on the finished products."

Further, respondent posits that under Revenue Regulations No. 17-67, specifically Section 1 paragraph 1 thereof, stemmed leaf tobacco is considered as partially prepared tobacco within the ambit of Section 141 of the NIRC.

These contradictory points of view had already been raised by the same parties in earlier cases. The Court of Appeals, just recently, had settled the same controversy in **Commissioner of Internal Revenue vs. Fortune Tobacco Corporation,** CA-SP Nos. 38219 and 40313 (CTA Case Nos. 4587 and 4616) promulgated on January 30, 1998. We find it therefore significant to cite the more important and relevant portions of the said decision, thus:

> "There is no disputing the fact that stemmed leaf tobacco is not among the tobacco products expressly mentioned in Section 141. The issue, therefore, is whether or not Revenue Regulations No. 17-67 is valid insofar as it interprets the statutory term "partially prepared tobacco" so as to include stemmed leaf tobacco.
>
> It is an elementary principle of Administrative Law that in interpreting or implementing a provision of law, a government agency cannot go beyond the terms and provisions of the basic law. Much less can it go against the law itself. Administrative rules and regulations issued by a particular

department or agency must be in harmony with the provision of law and should be for the sole purpose of carrying into effect the statutory provisions which it is construing or implementing. An administrative agency cannot extend, diminish, or otherwise amend the general provision of law (Fernando Juan vs. Musngi, 155 SCRA 133 [1987]; U.S. vs. Tupasi Molina, 29 Phil. 119; Director of Forestry vs. Munoz, 23 SCRA 1183 [1968]; Gonzalo Sy vs. Juinio, 127 SCRA 342 [1984]).

There are limitations to the rule making power of administrative agencies. When Congress authorizes an administrative body to promulgate rules and regulations to implement given legislation, all that is required is that the regulation must not contravene the statute, but must conform to the standards it prescribed (Tayug Rural Bank vs. Central Bank, 146 SCRA 120 [1986]; Del Mar vs. Philippine Veterans Administration, 52 SCRA 340 [1973]).

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In case of discrepancy between the basic law and a rule or regulation issued to implement it, the basic law prevails. The regulation cannot go beyond the provisions and terms of the basic law (Shell Philippines Inc. vs. Central Bank, 162 SCRA 628 [1988]).

After a careful study of all aspects of the law and the revenue regulation involved in this case, We come to the conclusion that the Commissioner of Internal Revenue has not engaged in mere interpretation but has gone into unauthorized modification or amendment of the law. Only Congress can do this. Section 2(M)(1) of Revenue Regulations No. 17-67 is, therefore, ultra vires and invalid.

Section 137 of the Tax Code, earlier cited, expressly defines "stemmed leaf tobacco" and excludes it from payment of the tax when sold in bulk as raw material one manufacturer directly to another. While this particular

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section provides for removal of tobacco products without prepayment of tax, it is significant that the Tax Code defines and classifies stemmed leaf tobacco under its Section 137. When Revenue Regulations No. 17-67 undertakes to classify stemmed leaf tobacco under Section 141 in a manner different from the way it is treated in Section 137, it is no longer engaged in mere classification. It is already adding something to the law not in consonance with what the law itself specifically provides but contrary to it. It is not only engaged in amendment but in amendment contrary to a specific provision of the same law.

The petitioner argues that Section 137 is for one tax purpose while Section 141 is for another. The fact is that the reason for one provision is also present in the other and must, therefore, be treated in the same light.

Section 141 of the Tax Code specifically excludes "fine cut shorts and refuse, clippings, cuttings stems and sweepings of tobacco resulting from the handling or stripping of whole leaf tobacco" from the 75 centavos per kilogram tax when disposed of or sold. The condition in the statute is that the above must be exported or used in the manufacture of other tobacco products. The reason for the exclusion is that the excise tax will eventually be paid on the finished product.

The same reason applies to stemmed leaf tobacco which is intended solely as a raw material in the manufacture of cigarettes and other tobacco products. After the cigarettes are manufactured, excise taxes will be paid. In effect, what the petitioner has provided in the disputed regulation is double taxation - the payment of excise taxes on the raw material and later, the payment of excise taxes on the manufactured product. Double taxation must be specifically and clearly provided by law. It cannot be imposed by administrative rule-making

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body. If specifically excluded under the last paragraph of Section 141, taxes cannot be included under paragraph 2 of the same section by a mere interpretation of the petitioner.

It is elementary that any taxes not specifically imposed by law cannot be mandated on the strength of an administrative regulation which purports to implement the said law. Only Congress, not the BIR, can provide for additional taxes. Revenue Regulations No. 17-67 is correct when it provides for the procedure in enforcing the statute. It can state the rules, taxation-wise, on securing permits, putting up factories and machineries, procuring raw materials, recording production, and disposing of the finished product. But the petitioner's powers are limited to procedure and implementation and not substantive law which seeks to add new taxes in addition to those specifically taxed under the law. This is especially true when the particular product being taxed by regulation is expressly excluded from taxes in another section of the same law and also in another law. The petitioner is arrogating powers to itself which it does not possess.

The argument that stemmed leaf tobacco used as raw material is exempt from taxation only when it is from one L-7 manufacturer to another L-7 manufacturer suffers from the same infirmity. It is based on the BIR's own Revenue Regulation V-39 which add to the law something which is not there. Using its power of classification, the petitioner has ventured into an amendment and amplification of the basic law.

Section 141 taxes fine cut shorts and refuse, scraps, clippings, stems and sweepings but the unnumbered paragraph after Section 141(c) exempts these items if they are used in the manufacture of other tobacco products on which the excise tax will eventually be paid on the finished product.

The law defines and exempts certain raw materials on condition that excise taxes will eventually be paid on the finished manufactured product. The BIR has classified these raw materials in a restrictive manner - only from one L-7 to another L-7 when all that the law requires is that the excise taxes not collected at the start will eventually be paid once the tobacco product comes out in final form. For a wide variety of raw materials, there is double imposition by the BIR of excise taxes when the law obviously removes taxes at the start of the manufacturing process and imposes them only once - when the process is completed. Again, double taxation is valid but only when it is provided by statute. It cannot be imposed through an interpretative rule.

The petitioner's contention that the classification of stemmed leaf tobacco as "partially manufactured" tobacco under Revenue Regulations No. 17-67 prevails over the definition of processed tobacco under Rep. Act 698 is fanciful to say the least. Revenue Regulations No. 17-67 is not a basic law. It is simply an implementation of the statutory provision of the Tax Code. A mere regulation of a quasi-legislative agency cannot prevail over the express definition under a law passed by Congress itself. It is elementary that an administrative regulation cannot amend or repeal the express provisions of statutes enacted by Congress. How can the petitioner argue that an administrative regulation prevails over a statute or law?

The petitioner states that Sections 141 and 137 of the Tax Code must be read and construed together. It explains that under Section 141 stemmed leaf tobacco, being partially prepared tobacco is subject to specific tax. However, under Section 137 if the stemmed leaf tobacco is sold in bulk directly from one manufacturer to another in accordance with the conditions prescribed in Section 20(a) of Revenue Regulation No. V-39, it is exempt from specific tax. It is very

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> obvious that it is not the Tax Code which taxes on one hand and exempts from taxes on the other hand the tobacco involved. It is the addition of a definition of partially manufactured tobacco which clashes with the law itself and the regulatory conditions of the BIR which restrict the application of the law to an extremely limited class that form the basis of BIR action. The petitioner engages in legislation and then uses its own administrative or quasi-legislative powers to add a certain class of tax which is neither expressed nor contemplated in the basic law.
>
> We are aware of the ruling in Commissioner of Internal Revenue vs. La Suerte Cigar and Cigarette Factory, Inc., CA-G.R. SP No. 38107 issued on December 29, 1995.
>
> We note, however, that this Court in the case of La Suerte Cigar failed to take into account the limitations in the exercise of quasi-legislative powers by administrative agencies. True, the law in Sections 141 and 137 of the Tax Code contains the phrase "under such conditions as may be prescribed in the regulations of the Department of Finance." However, the power to prescribe regulations is not a carte blanche giving the BIR full discretionary authority to add to the law. It is not a roving commission. It is subject to established and basic principles of Administrative Law enunciated in scores of Supreme Court decisions. There is no discrepancy between the principles enunciated in this decision and in the La Suerte decision except that the latter stopped short and did not go into the powers of administrative agencies. If it had gone fully and far enough into the quasi-legislative powers of the Bureau of Internal Revenue, it would have arrived at conclusions fully consonant with our findings."

Verily, from the above ruling, it appears that the petitioner is entitled to the refund it claimed. But petitioner has first to show proof(s) that the aggregate amount of ₱274,738.50 allegedly collected by the BIR was actually received by it. In other words, petitioner must prove that indeed it paid the specific taxes during the month of September, 1994.

Petitioner made mention of several payments for the month of September, 1994. But no document(s) had been submitted for the Court to prove the same. Consequently, the Court has nothing to consider respecting the dates of payments, the amounts of stemmed leaf tobacco imported, the corresponding specific taxes assessed and collected, the confirmation receipts and payment orders as well as the amount of each payment.

It is enlightening to reproduce part of the proceedings of July 8, 1997 (TSN, pp. 12-15):

"ATTY. DEL CASTILLO

> Your Honors, we might not present another witness. Unless, the counsel for the respondent is willing to stipulate on one of his admissions on his answer, Your Honors, which I just told right now. "This is a claim for refund of specific taxes which were paid by the petitioner during the month of September 1994". In paragraph 2 of the answer, Your Honors, the respondent admits that the petitioner paid the amount of ₱274,730.50 (*sic*). But states that this was for the

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month of June 1994, Your Honors. If the respondent's counsel is willing to stipulate that this refers to the month of September 1994, I will no longer present another witness, Your Honors.

JUDGE ACOSTA

Atty. Tolentino?

ATTY. TOLENTINO

May we be given a little time to review the records, Your Honors.

JUDGE ACOSTA

Is that not included in the stipulation of facts?

ATTY. DEL CASTILLO

No, I have not included, Your Honors.

JUDGE ACOSTA

Do you have more facts which you want the respondent to admit also? So that, it will not be piecemeal anymore.

ATTY. DEL CASTILLO

No, not is it, Your Honors. In fact, I was planning to rest my case after this.

JUDGE ACOSTA

Only that figure?

ATTY. DEL CASTILLO

Yes, Your Honors.

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JUDGE ACOSTA

Why don't you examine it at the back. Can you wait for a while?

ATTY. DEL CASTILLO

Yes, Your Honors.

JUDGE ACOSTA

Are those payment pertains to September of 1994, not to June of 1994.

ATTY. TOLENTINO

Yes, Your Honors. We express our willingness to rectify the...

JUDGE ACOSTA

Portion of your answer pertaining to that?

ATTY. TOLENTINO

Yes, Your Honors.

JUDGE ACOSTA

So?

ATTY. DEL CASTILLO

One more admission, Your Honors. Will the counsel for the respondent admit that the stemmed leaf tobacco which the petitioner imports is used to manufacture cigarettes.

ATTY. TOLENTINO

Yes, Your Honors, we are willing to admit that.

JUDGE ACOSTA

All right.

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At first blush, it seems that respondent admits that the amount of P274,738.50 was collected from petitioner. But to be fair to the respondent, We must read said portion in relation to the whole paragraph of No. 2 in the answer, to wit:

> "2. ADMIT the allegations in paragraph 3 of the petition that the Commissioner of Internal Revenue collected from LA SUERTE the amount of P274,738.50 as specific taxes due on bulk purchases of stemmed leaf tobacco from foreign tobacco manufacturers or suppliers in June 1994 but SPECIFICALLY DENY the rest of the allegations therein as well as the allegations in paragraphs 4, 5 and 6 for lack of knowledge or information to form a belief as to the truth thereof. <u>Whether or not the aforestated amount allegedly representing payment of specific taxes on imported tobacco for the year 1994 were actually received by the government is yet subject to verification.</u> (Underscoring supplied.).

Moreover, as can be gleaned from the transcript of stenographic notes, respondent's counsel expressed willingness only to rectify the mistake pertaining to the month involved. There is no clear showing that he agreed to such admission of fact.

Settled is the rule that in an action for tax refund, the burden of proof is on the taxpayer to establish its right to the refund. (**Caltex [Phils.] Inc. vs. Commissioner of Internal Revenue, CTA Case No. 2871,**

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january 29, 1986; Citibank N.A. [Phil. Br.] vs. Commissioner of Internal Revenue, CTA Case No. 4258, April 11, 1994). Herein petitioner has failed to convince the Court that it is entitled to the refund sought.

WHEREFORE, premises considered, this Court has no recourse but to **DENY** the instant petition for review for failure to substantiate.

SO ORDERED.

AMANCIO Q. SAGA
Associate Judge

WE CONCUR:

ERNESTO D. ACOSTA
Presiding Judge

RAMON O. DE VEYRA
Associate Judge

CERTIFICATION

I hereby certify that the above decision was reached after due consultation with the members of the Court of Tax Appeals in accordance with Section 13, Article VIII of the Constitution.

ERNESTO D. ACOSTA
Presiding Judge

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