REPUBLIC OF THE PHILIPPINES
Court of Tax Appeals
QUEZON CITY

SECOND DIVISION

PETRON CORPORATION,
Petitioner,

C.T.A. CASE NO. 6423

Members:

- versus -

CASTAÑEDA, JR., *Chairperson*
UY, *and*
PALANCA-ENRIQUEZ, *JJ.*

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:

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DECISION

UY, *J*.:

Before Us is the 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 taxable years 1995 to 1998 in the total amount of **SEVEN HUNDRED THIRTY NINE MILLION THREE THOUSAND THIRTY SIX AND 32/100 PESOS (P739,003,036.32)** inclusive of the surcharge of P159,460,900.00 and interest of P260,620,335.32, 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.

THE PARTIES

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 provisions of the Omnibus Investments Code of 1987 (E.O. 226) under Certificates of Registration No. 89-1037 and D95-136.[1] 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, with office address at the BIR Building, Diliman, Quezon City.

THE FACTS

As culled from the records and as agreed upon by the parties in their Joint Stipulation of Facts and Issues, these are the facts of the case.

During the period covering the taxable years 1995 to 1998, petitioner had been an assignee of several Tax Credit Certificates (TCCs) from various BOI-registered entities for which petitioner utilized in the payment of its excise tax liabilities for the taxable years 1995 to 1998. The transfers and assignments of the said TCCs were approved by the Department of Finance's One Stop Shop Inter-Agency Tax Credit and Duty Drawback Center (DOF Center), 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

[1] Par. 3, Petition for Review, Records, p. 2.

Revenue (BIR).[2]

Taking ground on a BOI letter issued on May 15, 1998 which states that *"hydraulic oil, penetrating oil, diesel fuels and industrial gases are classified as supplies and considered the suppliers thereof as qualified transferees of tax credit",*[3] petitioner acknowledged and accepted the transfers of the TCCs from the various BOI-registered entities.

Petitioner's acceptance and use of the TCCs as payment of its excise tax liabilities for the taxable years 1995 to 1998, had been continuously approved by the DOF as well as the BIR's Collection Program Division through its surrender and subsequent issuance by the Assistant Commissioner of the Collection Service of the BIR of the Tax Debit Memos (TDMs).[4]

On January 30, 2002, respondent issued the assailed "Assessment" against petitioner for deficiency excise taxes for the taxable years 1995 to 1998, in the total amount of P739,003,036.32, inclusive of surcharges and interests,[5] based on the ground that the TCCs utilized by petitioner in its payment of excise taxes have been cancelled by the DOF for having been fraudulently issued and transferred, pursuant to its EXCOM Resolution No. 03-05-99. Thus, petitioner, through letters dated August 31, 1999 and September 1, 1999, was required by the DOF Center to submit copies of its sales invoices and delivery receipts showing the consummation of the sale

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[2] Par. 4, Joint Stipulation of Facts & Issues, Records, p. 128.
[3] Diamond Knitting Corporation, Fiber Technology Corporation, Filstar Textile Industrial Corporation, Alliance Thread Co., Inc., Allstar Spinning, Inc., FLB International Fiber Corporation, Jantex Philippines, Inc., Jibtex Industrial Corporation, Master Colour System Corporation and Spintex International, Inc.
[4] Par. 5, Joint Stipulation of Facts & Issues, Records, p. 128.
[5] Par. 1, Joint Stipulation of Facts & Issues, Records, p. 126.

transactions to certain TCC transferors.[6]

Instead of submitting the documents required by the respondent, on February 27, 2002, petitioner filed its protest letter to the "Assessment" on the grounds, among others, that:[7]

a. The BIR did not comply with the requirements of Revenue Regulations 12-99 in issuing the "assessment" letter dated January 30, 2002, hence, the assessment made against it is void;

b. The assignment/transfer of the TCCs to petitioner by the TCC holders was submitted to, examined and approved by the concerned government agencies which processed the assignment in accordance with law and revenue regulations;

c. There is no basis for the imposition of the 50% surcharge in the amount of P159,460,900.00 and interest penalties in the amount of P260,620,335.32 against it;

d. Some of the items included in the "assessment" are already pending litigation and are subject of the case entitled "Commissioner of Internal Revenue vs. Petron Corporation," C.A. GR SP No. 55330 (CTA Case No. 5657) and hence, should no longer be included in the "assessment"; and

e. The assessment and collection of alleged excise tax deficiencies sought to be collected by the BIR against petitioner through the January 30, 2002 letter are already barred by prescription under Section 203 of the National Internal Revenue Code.

On 27 March 2002, respondent, through Assistant Commissioner Edwin R. Abella served a Warrant of Distraint and/or Levy on petitioner to enforce payment of the P739,003,036.32 tax deficiencies.[8]

Respondent allegedly served the Warrant of Distraint and/or Levy against petitioner without first acting on its letter-protest. Thus, construing the Warrant of Distraint and/or Levy as the final adverse decision of the BIR on its

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[6] Par. 10, Joint Stipulation of Facts & Issues, Records, p. 129.
[7] Par. 12 – 12.5, Joint Stipulation of Facts & Issues, Records, pp. 129-130.
[8] Records, p. 37.

protest of the assessment, petitioner filed the instant petition before this Honorable Court on April 2, 2002.

On April 30, 2002, respondent filed his Answer, raising the following as his Special and Affirmative Defenses:

6. In a post-audit conducted by the One-Stop Inter-Agency Tax Credit and Duty Drawback Center (Center) of the Department of Finance (DOF), pursuant to the Center's Excom Resolution No. 03-05-99, it was found that TCCs issued to Alliance Thread Co., Inc., Allstar Spinning, Inc., Diamond Knitting Corp., Fiber Technology Corp., Filstar Textile Industrial Corp., FLB International Fiber Corp., Jantex Philippines, Inc., Jibtex Industrial Corp., Master Colour System Corp. and Spintex International, Inc. were fraudulently obtained and were fraudulently transferred to petitioner. As a result of said finding, the TCCs and the Tax Debit Memos (TDMs) issued by the Center to petitioner against said TCCs were cancelled by the DOF;

7. Prior to the cancellation of the aforesaid TCCs and TDMs, petitioner had utilized the same in payment of its excise tax liabilities. With such cancellation, the TCCs and TDMs 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 DOF of the aforesaid TCCs and TDMs has the presumption of regularity upon which respondent may validly rely;

9. Petitioner was informed by the DOF of the post-audit conducted on the TCCs and was given the opportunity to submit documents showing that the TCCs were transferred to it in payment of petroleum products allegedly delivered by it to the TCC transferors upon which the TCC transfers were approved, with the admonition that failure to submit the required documents would result in the cancellation of the transfers. Petitioner was also informed of the cancellation of the TCCs and TDMs and the reason for their cancellation;

10. Since petitioner is deemed not to have paid its excise tax liabilities, a pre-assessment notice is not required under Section 228 of the Tax Code;

11. The letter dated January 20, 2002 (should be January 30,

2002), demanding payment of petitioner's excise tax liabilities explicitly states the basis for said demand, i.e., the cancellation of the TCCs and TDMs;

12. The government is never estopped from collecting legitimate taxes due to the error committed by its agents (Visayas Cebu Terminal Inc., vs. Commissioner of Internal Revenue, 13 SCRA 257; 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 as payment of its excise tax liabilities turned out to be a mistake after the post-audit was conducted. Hence, said payments were void and the excise taxes may be validly collected from petitioner;

13. As found in the post-audit, petitioner and the TCC transferors committed fraud in the transfer of the TCCs when they made appear that the transfers were in consideration for the delivery of petroleum products by petitioner to the TCCs transferors, for which reason said transfers were approved by the Center, when in fact there were no such deliveries;

14. Petitioner used the TCCs fraudulently obtained and fraudulently transferred 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;

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

16. Since petitioner willfully filed fraudulent returns with intent to evade tax, the prescriptive period to collect the tax is ten (10) years from the discovery of the fraud pursuant to Section 222 of the Tax Code; and

17. The case pending in the Court of Appeals (CA-G.R. Sp. No. 55330 [CTA Case No. 5657]), and the case at bar have distinct causes of action. The former involves the invalid transfers of the TCCs to petitioner on the theory that it is not a qualified transferee thereof, while the latter involves the fraudulent procurement of said TCCs and the fraudulent transfers thereof to petitioner.

However, on November 12, 2002, respondent filed a Manifestation informing this Court that on May 29, 2002, it had reduced the amount of deficiency excise taxes to P720,923,224.74 as a result of its verification that some of the TCCs which formed part of the original "Assessment" were already included in a case previously filed with this Court. In effect, the amount of deficiency excise taxes is recomputed as follows:

Transferor	Basic Tax	Surcharge	Interest	Total
Alliance Thread Co. Inc.	P 12,078,823.00	P 6,039,411.50	P 16,147,293.21	P 34,265,527.71
Allstar Spinning, Inc.	37,265,310.00	18,632,655.00	49,781,486.95	105,679,451.95
Diamond Knitting Corporation	36,764,587.00	18,382,293.50	49,264,758.35	104,411,638.85
Fiber Technology Corp.	25,300,911.00	12,650,455.50	34,295,655.90	72,247,022.40
Filstar Textile Corp.	40,767,783.00	20,383,891.50	54,802,550.16	115,954,224.66
FLB International Fiber Corp.	25,934,695.00	12,967,347.50	34,977,257.14	73,879,299.64
Jantex Philippines, Inc.	12,036,192.00	6,018,096.00	15,812,547.24	33,866,835.24
Jibtex Industrial Corp.	15,506,302.00	7,753,151.00	20,610,319.52	43,869,772.52
Master Colour System Corp.	33,333,536.00	16,666,768.00	44,822,167.06	94,822,471.06
Spintex International Inc.	14,912,408.00	7,456,204.00	19,558,368.71	41,926,980.71
Total	**P253,900,547.00**	**P126,950,273.50**	**P340,072,404.24**	**P720,923,224.74**

During the pendency of the case, but after respondent had already submitted his Formal Offer of Evidence for this Court's consideration, he filed an "*Urgent Motion to Reopen Case*" on August 24, 2004 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 transfer of the subject TCCs. Respondent submits that it is imperative on his part to do so considering that, without necessarily admitting that the evidence presented in the case of Pilipinas Shell Petroleum Corporation vs. Commissioner of

Internal Revenue,[9] to prove fraud is not clear and convincing, he may suffer the same fate that had befallen upon therein respondent when this Court held, among others, 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."

An *"Opposition to Urgent Motion to Reopen Case"* was filed by petitioner on September 3, 2004 contending that to sustain respondent's motion would "smack of procedural disorder and spawn a reversion of the proceedings. While litigation is not a game of technicalities, it is a truism that every case must be presented in accordance with the prescribed procedure to insure an orderly administration of justice."

On October 4, 2004, this Court resolved to grant respondent's Motion and allowed respondent to present additional evidence in support of his arguments, but deferred the resolution of respondent's original Formal Offer of Evidence until after the respondent has terminated his presentation of evidence. Subsequent to this Court's Resolution, respondent then filed on October 20, 2004, a Request for the Issuance of *Subpoena Duces Tecum* to the Executive Director of the Center or his duly authorized representative, and on October 21, 2004, a *Subpoena Ad Testificandum* to Ms. Elizabeth R. Cruz, also of the Center.

Petitioner filed a *"Motion for Reconsideration (Re: Resolution dated October 4, 2004)"* on October 27, 2004, with respondent filing his *"Opposition"* on November 4, 2004, and petitioner subsequently filing its *"Reply to*

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[9] CTA Case No. 6003, August 2, 2004.

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Opposition" on December 20, 2004. Petitioner's motion was denied by this Court in a Resolution dated February 28, 2005 for lack of merit.

On March 18, 2005, petitioner filed an *"Urgent Motion to Revert Case to the First Division"* with respondent's "Manifestation" filed on April 6, 2005 stating that "the question of which Division of this Honorable Court shall hear the instant case is an internal matter which is better left to the sound discretion of this Honorable Court without interference by a party litigant". On April 28, 2005, this Court denied the Motion of petitioner for lack of merit.

On November 7, 2005, the Court finally resolved respondent's *"Formal Offer of Evidence"* filed on May 7, 2004 and *"Supplemental Formal Offer of Evidence*" filed on August 25, 2005. On November 22, 2005, respondent filed a *"Motion for Partial Reconsideration"* of the Court's Resolution to admit Exhibits 31 and 31-A on the ground that he already submitted and offered certified true copies of said exhibits, which the Court granted in its Resolution dated January 19, 2006.

However, on February 10, 2006, respondent filed a *"Motion to Amend Formal Offer of Evidence"* praying that he be allowed to amend his formal offer since some exhibits, although attached thereto, were inadvertently not mentioned in the Formal Offer of Evidence. Petitioner's *"Opposition"* was filed on March 14, 2006. This Court granted respondent's motion in the Resolution dated April 24, 2006 and considering that the parties already filed their respective Memoranda, this case was then considered submitted for decision.

On May 16, 2006, however, respondent filed an *"Omnibus Motion"* praying that this Court take judicial notice of the fact that the TCCs issued by the Center, including the TCCs in this instant case, contained the standard

"Liability Clause"[10] and that the case be consolidated with CTA Case No. 6136, on the ground that both cases involve the same parties and common questions of law or fact. An *"Opposition/Comment on Omnibus Motion"* was filed by petitioner on June 26, 2006, and *"Reply to Opposition/Comment"* was filed by respondent on July 17, 2006.

In a Resolution promulgated on September 1, 2006, this Court granted respondent's motion only insofar as taking judicial notice of the fact that each of the dorsal side of the TCCs contains the subject "liability clause", but denied respondent's motion to consolidate considering that C.T.A. Case No. 6136 was already submitted for decision on April 24, 2006.

THE ISSUES

The issues as stipulated by the parties are as follows:

1. Whether or not the cancellation by the Secretary of Finance of the TDMs issued to petitioner and their related TCCs and TCC transfers, which were used by petitioner in the payment of excise taxes, has the effect of voiding said payment;

2. Whether or not Petron was aware of any fraudulence in the obtainment and/or assignment by the TCC holders of the TCCs or of any defect or flaw thereon;

3. Whether or not the TCCs transferred to petitioner were fraudulently obtained by the entities/grantees thereof and subsequently fraudulently transferred by them to petitioner;

4. Whether or not the Commissioner of Internal Revenue is estopped from questioning and invalidating Petron's payment of excise taxes thru the use of the TCCs which the BIR continuously approved after the TCCs had been verified and validated by the DOF Center;

5. Whether or not the assessment and collection of alleged excise tax deficiencies for 1995-1998 sought to be collected

[10] Liability Clause. : "Both the TRANSFEROR and the TRANSFEREE shall be jointly and severally liable for any fraudulent act or violation of the pertinent laws, rules and regulations relating to the transfer of this TAX CREDIT CERTIFICATE."

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by the BIR against Petron Corporation through the January 30, 2002 letter are already barred by prescription under Section 203 of the National Internal Revenue Code (NIRC);

6. Whether or not the use by petitioner of the TCCs approved by the DOF and the BIR and transferred to petitioner in payment of excise taxes constitute fraud with intent to evade tax; and

7. Whether or not there is compliance with the requirement under Section 228 of the Tax Code that the taxpayer shall be informed of the law and of the facts on which the assessment is made.

THE COURT'S RULING

Before delving into the above-stipulated issues, pertinent provisions of law, rules and regulations and agreements are hereunder quoted for ready reference, 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 certificate 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.

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(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 <u>used</u> 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.)*

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

"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.

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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)*

<u>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</u>

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

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I.) Henceforth, **all tax credit certificates**, except for net local content (NCL) 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.)*

II.) 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.

III.) 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 were issued."

d. <u>BOI Letter dated May 15, 1990</u>

"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."

Petitioner submits that the validity of its payments of excise taxes through the use of the TCCs assigned to it had been resolved and settled by this Court in favor of petitioner in the case of Petron Corporation vs. Commissioner of Internal Revenue.[11] Petitioner avers that the factual circumstances and issues, which were resolved in the said case, are similar, if not the same, as those found in this instant case. Necessarily, the doctrine or ruling therein finds relevance and application in the present case.

Petitioner further alleges that the subject TCCs assigned by Alliance Thread Co., Inc., Allstar Spinning, Inc., Diamond Knitting Corp., Fiber Technology Corp., Filstar Textile Corp., FLB International Fiber Corp., Jantex Philippines Inc., Master Colour System Corp., and Spintex International Inc. are all genuine. The report of the Court-commissioned Independent CPA, Ms. Lilian Linsangan, was presented by petitioner to help bolster this claim. Petitioner argues that the TCCs were assigned to it in accordance with the requirements of law and such assignments were duly approved by the appropriate government agencies, as evidenced by the fact that petitioner's utilization of the TCCs in its payments of excise taxes were continuously accepted by the Collection Program Division of the BIR.

Moreover, petitioner asserts that it had fulfilled its obligation to issue credit notes to the assignors under the Deeds of Assignment entered into between itself and the assignors, 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 likewise confirmed by the audit report of the Court-commissioned Independent Certified Public Accountant, Ms. Lilian S. Linsangan.

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[11] CTA Case No. 5657, July 23, 1999.

Petitioner furthermore 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; and that, petitioner is not aware of any fraudulence in obtaining the TCCs nor is it aware of any flaw or defect on the subject TCCs. Accordingly, the tedious procedure for the assignment of the TCCs, which consists of three layers of review by the different government entities, clearly dispels any fraudulent transfer of the TCCs. Undeniably, petitioner insists that it is an innocent purchaser for value of the TCCs, for which, it has been ruled that an innocent purchaser for value or a purchaser in good faith is one who has no knowledge of any defect or lack of title of the vendor.[12] Fraud must be established by clear and convincing evidence.

Petitioner disputed the affidavits presented by the general managers of the assignor-corporations, which attested to the non-delivery of fuel and other petroleum products to them on the ground that these are all hearsay. As these general managers were never presented to affirm their affidavits, the petitioner as well as this Court were never given the opportunity to cross-examine them and test their credibility.

On the other hand, respondent is unwavering in his argument that the TCCs were fraudulently obtained by petitioner. Allegedly, the post-audit on the subject TCCs 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

[12] Dela Merced vs. GSIS, G.R. NO. 140398, September 11, 2001.

effectively render the TCCs *void ab initio.*

Respondent further maintains that it must be shown that petitioner, to be a qualified transferee of TCCs, is a supplier of petroleum products to the TCC transferors. Upon post-audit, considering the finding that petitioner did not make any delivery of fuel and other petroleum products to the assignor-companies of the TCCs as agreed upon in their Supply Agreements, it cannot be concluded that petitioner is indeed a supplier of petroleum products. This allegedly was confirmed by the failure of petitioner to submit to the Center copies of the sales invoice and delivery receipts showing consummation of said transaction.

Moreover, respondent reasoned that, although petitioner presented evidence showing that in consideration of the transfer of the TCCs, it issued credit notes for petroleum products to the TCC transferors which, in turn, assigned the credit notes to other entities to whom petitioner delivered the petroleum products, such assignment made by the entities, other than petitioner, was never stipulated in the Deeds of Assignment. And in the absence of such stipulation, the Center could not have known if there was indeed any delivery made other than to the TCC transferors themselves. Since petitioner did not actually supply petroleum products to the TCC transferors, respondent believes that it did not become a qualified transferee. Consequently, the TCC transfers were not valid. According to respondent, 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 thereof made the transfer fraudulent.

This Court agrees with respondent.

We rule that 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.

The findings of the DOF that the TCCs do no have monetary value is undisputed. Consequently, the effect would be non-payment of respondent's excise taxes corresponding to the value of the TCCs supposedly used for payment simply because payment can only occur if the instrument used to discharge an obligation represented its stated value. It bears stressing that 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.

Relevant thereto, the Supreme Court explained the matter in this wise:

> "Attention must be given to the fact that taxes are the lifeblood of the nation through which the government agencies continue to operate and with which the State effects its functions for the welfare of its constituents. It is also settled that taxes are the lifeblood of the government and their prompt and certain availability is an imperious need. So then, the determination of the validity or invalidity of the TCCs cannot be regarded as a prejudicial issue that must first be resolved with finality in the Criminal Cases filed before the Sandiganbayan. The Government should not and must not await the result of the criminal proceedings in the Sandiganbayan before it can collect the outstanding customs duties and taxes of the petitioner for such will unduly restrain the Government in doing its functions. The machineries of the Government will not be able to function well if the collection of taxes will be delayed so much so if its collection will depend on the outcome of any criminal proceedings on the guise that the issue of collection of taxes is a prejudicial issue that need to be first resolved before enforcing its collection.

> **Therefore, it is the obligation of the petitioner to make good its obligation by paying the customs duties and taxes, which remain unpaid by reason of the cancellation of the subject TCCs for having been found as fake and spurious. It should not make the Government suffer for its own misfortune**."[13] *(Emphasis supplied)*

It must be emphasized at this point 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 in the TCC, which states that **"This Tax Credit is issued subject to: 1. Post-audit x x x".**

Hence, it cannot be over-emphasized that the acceptance by the petitioner of the subject TCCs is considered a contract entered into by and between the issuing authority and the petitioner itself. And as with any other valid contract, the same is subject to certain conditions binding to both parties. In other words, when petitioner obtained the TCCs, it was bound by the conditions expressly set forth therein. Logically, a party entering into a contract must necessarily be aware of the conditions it is to be subjected to before agreeing to be a party thereto, more so, if the said contract concerns huge amounts of taxes, like in this instant case. Simply put, it cannot be said that petitioner was unaware of the specific condition of "post-audit" and the consequences, which may arise after such 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

[13] Proton Pilipinas Corporation vs. Republic of the Philippines, represented by the Bureau of Customs, G.R. No. 165027, October 16, 2006.

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> 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.[14]

In view of the foregoing, it is clear 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 whether or not the holder of the TCCs is qualified to the issuance of the same. 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.

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. Indubitably, it is mandatory that the claimants for tax credits export their products. 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. Apparently, the bases for the approval of the TCCs were spurious export documents. This conclusion arrived at was

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[14] 8 Manresa 130-131, cited on page 140, Civil Code of the Philippines, Tolentino, 1962 ed., Vol. IV.

grounded on the fact of the excessively or impossibly high amounts of the tax credits per export sales of the assignor/transferor-companies ratios. The ratios of the amount of TCCs to the amount of sales, which was computed by dividing the average yearly TCC by the average yearly sales as indicated in the "Schedule of Tax Credit Certificates/Sales Ratio",[15] were way above the industry average of 13%. This clearly shows that the volume of export sales declared to the Center on the basis of which the TCCs were issued, was fake.

Moreover, it was concluded, among others, that the transferor/assignor entity Diamond Knitting Corporation was not in operation by virtue of a Cease and Desist Order[16] issued by the Pollution Adjudication Board on February 18, 1993, yet it was granted TCCs in the amount of P168,080,709.00 from 1993 to 1998. Also, in the case of Spintex International, Inc., verification of its export documents with the Bureau of Customs revealed the absence of Export Declarations, Authority to Load and Inspector Certificates of Loading.[17] Likewise, the Center's findings[18] disclosed that the transferors could not have exported their registered capacity of yarns and threads considering that their reported cost of machinery and equipment, per their Audited Financial Statements, obviously could not produce that much yarn and thread.

In addition, the affidavits[19] from the general managers of the transferor/assignor entities indicated 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

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[15] Exhibit "13".
[16] Exhibits "5-C" and "5-C-1".
[17] Exhibits "12-H" and "12-H-1".
[18] Exhibits "2-A", "3-A", "5-A", "6-A", "7-A", "8-A", "9-A", "10-A", and "11-A".
[19] Exhibits "2-F", "3-F", "4-E", "6-F", "7-F", "8-F", "9-F", "10-F", and "11-F".

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declared to the Center, on the basis of the TCCs issued, were false. Effectively, the post-audit conducted by the Center resulted in a finding of fraud in the transfer of the subject TCCs.

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." In the case at bench, post-audit disclosed that during the period covering 1995 to 1998, there were no deliveries of fuel and other petroleum products from petitioner to the transferor/assignor-companies as stated in their Supply Agreement. This is confirmed by the Report[20] submitted by the Court-commissioned Independent CPA dated May 6, 2003 as shown on Annex 12,[21] which revealed that most of the fuel products which were supposed to be delivered to the transferors/assignor-companies were delivered instead to Duracom, Petrotrade, Royale Fishing, and Filsyn.[22] Also, some of the fuel products which were supposed to be delivered to Fiber Technology were delivered to Filsyn;[23] those supposedly for Filstar Textile were delivered to Diamond Knitting Corporation, Jantex Philippines and Alliance Thread Co., Inc.;[24] and those supposedly for Master Colour were delivered instead to Jantex Philippines, Alliance Thread and Fiber Technology.[25]

Respondent's Bureau (the BIR), being a subordinate government

[20] Exhibit "A".
[21] Annex "12" of Exhibit "A".
[22] Exhibits "M" to "M-17".
[23] Exhibits "M-4" to "M-5".
[24] Exhibit "M-7".
[25] Exhibits "M-11" to "M-14".

agency, is bound to adopt the findings of the DOF considering that the latter is the agency, which actually conducts 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 the present case, circumstances are brim with fraud, both as to the issuance of the subject TCCs and their transfer to petitioner.

As regards petitioner's liability, 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", necessarily applies in this case. When the petitioner utilized the TCCs for its payment of excise taxes at the time when the post-audit was not yet conducted nor finalized, it did so at its own risk. Petitioner is therefore liable for the loss of the thing due even if it was caused by the fault of only one party and this is regardless of whether or not there was knowledge on the part of the petitioner of the fraud committed. It must be stressed that the validity and propriety of the TCCs in question so as 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, petitioner, though it may have allegedly obtained the same in good faith, is inevitably bound by the outcome by virtue of the express provisions stated on the TCCs.

Petitioner's arguments regarding the ground of estoppel deserve scant consideration. "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."[26] In stressing the rationale of 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 governmental functions the State cannot be estopped by the neglect or omissions of its agents. Nowhere is this more true than in the filed of taxation."[27]

Furthermore, Administrative Order No. 266 which created the Center, specifically provides that 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

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[26] Commissioner of Internal Revenue vs. Armando Abad-Republic Alcohol Distillery, G.R. No. L-19627, June 27, 1968; Commissioner of Internal Revenue vs. Procter & Gamble Philippine Manufacturing Corporation, G.R. No. L-66838, April 15, 1988.
[27] Commissioner of Internal Revenue vs. Armando Abad-Republic Alcohol Distillery, ibid.

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.

With regard to the issue of prescription, it is noteworthy that the "Assessment" came about because of the cancellation by the Center of the subject TCCs and TDMs due to the findings of fraudulent assignment and transfer of the same. Evidently, without such findings, there would have been no cancellation leading to the issuance of the "Assessment". And because of the cancellation of the TCCs and TDMs, regardless of whether or not petitioner was actually involved in the fraudulent transfers, the same resulted in the non-payment by petitioner of its excise taxes for the period covering 1995 to 1998. In this regard, as no payment was considered made, there is falsity and/or omission in the filing of the tax return, thus bringing about the applicability of the ten-year prescriptive period within which to issue an assessment from the discovery of the falsity or omission pursuant to Section 222 of the National Internal Revenue Code (NIRC) of 1997 which provides:

> **"SEC. 222. Exceptions as to Period of Limitation of Assessment and Collection of Taxes. -**
>
> (a) **In the case of a false or fraudulent return with intent to evade tax or failure to file a return, the tax may be assessed**, or a proceeding in court for the collection of such tax may be filed without assessment, **at any time within ten (10)**

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> **years after the discovery of the falsity, fraud or omission:** *Provided*, That in a fraud assessment which has become final and executory, the fact of fraud shall be judicially taken cognizance of in the civil or criminal action for the collection thereof." *(Emphasis supplied)*

Nonetheless, this Court rules that the fifty percent (50%) fraud surcharge should not be imposed. In the case of **Aznar vs. Court of Tax Appeals,**[28] the Highest Court elucidated this point in the following manner:

> "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 committing 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." *(Emphasis supplied)*

In the light of the foregoing jurisprudential pronouncement, petitioner cannot be made to pay the aforesaid fifty percent (50%) 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 utmost, petitioner appears to have been merely negligent in its acquisition of the controversial TCCs by failing to trace and investigate the validity of the same before obtaining them from the transferor/assignor entities. As the Highest Court held, "fraud cannot be

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[28] G.R. No. L-20569, August 23, 1974.

presumed but must be proven."

Lastly, anent the impositions of the twenty-five percent (25%) late payment surcharge per annum, and the twenty percent (20%) interest per annum imposed under Sections 248(A) and 249, respectively, of the NIRC of 1997, the same cannot be waived for they are meant to compensate the government for their inability to utilize the taxes during the time such taxes remain unpaid.

WHEREFORE, premises considered, the instant Petition for Review is hereby **DENIED** for lack of merit. Accordingly, petitioner is **ORDERED TO PAY** the respondent the reduced amount of **SIX HUNDRED MILLION SEVEN HUNDRED SIXTY NINE THOUSAND THREE HUNDRED FIFTY THREE AND 95/100 PESOS (P600,769,353.95),** representing petitioner's deficiency excise taxes for the taxable years 1995 to 1998, recomputed as follows:

Transferor	Basic Tax		25% Surcharge	20% Interest	Total
Alliance Thread Co. Inc.	P 12,078,823.00		P 3,019,705.75	P 13,456,077.68	P 28,554,606.43
Allstar Spinning, Inc.	37,265,310.00		9,316,327.50	41,484,572.46	88,066,209.96
Diamond Knitting Corp.	36,764,587.00		9,191,146.75	41,053,965.29	87,009,699.04
Fiber Technology Corp.	25,300,911.00		6,325,227.75	28,579,713.25	60,205,852.00
Filstar Textile Corp.	40,767,783.00		10,191,945.75	45,668,791.80	96,628,520.55
FLB International Fiber Corp.	25,934,695.00		6,483,673.75	29,147,714.28	61,566,083.03
Jantex Philippines, Inc.	12,036,192.00		3,009,048.00	13,177,122.70	28,222,362.70
Jibtex Industrial Corp.	15,506,302.00		3,876,575.50	17,175,266.27	36,558,143.77
Master Colour System Corp.	33,333,536.00		8,333,384.00	37,351,805.88	79,018,725.88
Spintex International Inc.	14,912,408.00		3,728,102.00	16,298,640.59	34,939,150.59
Total	**P253,900,547.00**	[29]	**P63,475,136.75**	**P283,393,670.20**	**P600,769,353.95**

In addition, petitioner is **ORDERED TO PAY** the respondent **TWENTY FIVE PERCENT (25%) LATE PAYMENT SURCHARGE AND TWENTY PERCENT (20%) DELINQUENCY INTEREST** per annum on the amount of **SIX HUNDRED MILLION SEVEN HUNDRED SIXTY NINE THOUSAND**

[29] Per Manifestation of respondent filed on November 12, 2002, Records, p. 138.

THREE HUNDRED FIFTY THREE & 95/100 PESOS (P600,769,353.95), computed from June 27, 2002[30] until the amount is fully paid.

SO ORDERED.

Erlinda P. Uy

ERLINDA P. UY
Associate Justice

WE CONCUR:

Juanito C. Castañeda, Jr.

JUANITO C. CASTAÑEDA, JR.
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
Chairperson

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[30] See Collection Letter of respondent dated May 29, 2002, Records, p. 142 and petitioner's protest-letter dated July 16, 2002, Records, pp. 147-152.

CERTIFICATION

Pursuant to Article VIII, Section 13 of the Constitution, and the Division Chairperson'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.

ERNESTO D. ACOSTA
Presiding Justice