REPUBLIC OF THE PHILIPPINES
Court of Tax Appeals
QUEZON CITY

SECOND DIVISION

MAERSK-FILIPINAS, INC., for and in behalf of A.P. Moller-Maersk A/S,
Petitioner,

- versus -

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

C.T.A. CASE NO. 6931

Members:

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

Promulgated:

JAN 09 2008
8:01 a.m.

x- x

DECISION

UY, *J.*:

This case involves the claim of petitioner Maersk Filipinas, Inc., for and in behalf of A.P. Moller-Maersk A/S, against respondent, Commissioner of Internal Revenue, seeking the refund or issuance of a tax credit certificate in the total amount of **SIXTY FOUR MILLION TWO HUNDRED EIGHTY FOUR THOUSAND FOUR HUNDRED FORTY TWO PESOS AND 42/100 (P64,284,442.42)**, representing its alleged erroneous payment of Philippine income taxes on Gross Philippine Billings for the year 2001.

THE FACTS

Petitioner Maersk Filipinas Inc. is a corporation duly organized and existing under the laws of the Philippines, engaged in business as a shipping agent. Its principal office address is at 51st Floor, PBCom Building, Ayala Avenue corner Rufino St., Makati City.

A.P. Moller-Maersk A/S is a corporation organized and existing under the laws of the Kingdom of Denmark, engaged in business as an international shipping carrier.

Respondent, on the other hand, is the Commissioner of Internal Revenue, vested with the power to decide, approve, and grant refunds or tax credits of overpaid internal revenue taxes as provided by law. He holds office and may be served with summons, orders, pleadings, and other processes at the Bureau of Internal Revenue (BIR) National Office, BIR Building, Agham Road, Diliman, Quezon City.

For the taxable year 2001, AP Moller-Maersk A/S allegedly generated gross sales in the amount of P4,285,629,492.00, as reported on its Annual Income Tax Return filed by petitioner on April 16, 2002 via electronic filing under Reference Number 050200000002452.[1] Although international carriers are generally subject to the rate of two and a half percent (2.5 %) on income tax based on Gross Philippine Billings[2], petitioner made the aforementioned payments on the firm assertion that A.P. Moller-Maersk A/S, being a resident of the Kingdom of Denmark, is entitled to the preferential rate of one and a

[1] Exhibit "S".
[2] Sec. 28 (A)(3), National Internal Revenue Code of 1997.

half percent (1.5%) tax rate in accordance with Section 8(2)(a) of the RP-Denmark Tax Treaty.

Based on this reliance, petitioner filed and paid the corresponding income taxes on Gross Philippine Billings at the special rate of 1.5 %[3], to wit:

Quarters	**Gross Income Reported**	**Income Tax Based on 1.5% of Gross Sales/Income**	**Date Paid**
1st 2001	829,850,510.00	12,447,757.65	May 29, 2001
2nd 2001	1,097,824,235.00	16,467,363.53	Aug 28, 2001
3rd 2001	1,210,119,831.00	18,151,797.47	Nov 28, 2001
4th 2001	1,147,834,918.00	17,217,523.77	April 16, 2001
Total	**4,285,629,494.00**	**64,284,442.42**	

However, on the belief that residents of Cyprus are exempt from the payment of Philippine income taxes on profits derived from Philippine sources on their shipping operations pursuant to Article 12(1) of the *"The Agreement Between the Government of the Republic of the Philippines and the Government of the Republic of Cyprus on Merchant Shipping"*[4], petitioner filed an administrative claim for refund or issuance of a tax credit certificate[5] in the amount of P64,284,442.42, representing its erroneous payment of A.P. Moller-Maersk A/S' income taxes for the taxable year 2001. Petitioner argues that A.P. Moller-Maersk A/S is entitled to a complete exemption of Philippine income tax pursuant to the "most favored nation clause" provided under Article 8(2)(b) of the RP-Denmark Tax Treaty. And to toll the running of the

[3] Exhibits "J", "L", "N", and "S".
[4] Dated September 7, 1984, and entered into force on June 6, 1985.
[5] Exhibit "I".

two-year prescriptive period within which to file a claim for refund, petitioner then elevated this matter to this Court by way of a Petition for Review filed on April 13, 2004[6].

On June 14, 2004, respondent filed his Answer, raising the following as his Special and Affirmative Defenses, to wit:

> "4. He reiterates and pleads the preceding paragraph of this answer as part of his Special and Affirmative Defenses;
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> 5. Petitioner's alleged claim for refund is subject to administrative investigation/examination by the respondent;
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> 6. Section 28(A)(3)(b) provides that an international carrier doing business in the Philippines, as in the case of the petitioner, shall pay a tax of two and one-half percent (2½%) on its "Gross Philippine Billings". Gross Philippine Billings has been defined as gross revenue whether for passenger, **cargo** or mail originating from the Philippines up to final destination, regardless of the place of sale or payments of the passage or freight documents.
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> 7. As held in the case of *Commissioner of Internal Revenue v. British Overseas Airways Corp., et.al.*, 149 SCRA 395:
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>> "The **source of an income** is the property, **activity** or service that produced the income. For the source of income to be considered as coming from the Philippines, it is sufficient that the source of income is derived from activity within the Philippines. xxx (emphasis supplied)
>
> The instant case is analogous to the case of *British Overseas Airways Corp. (BOAC)*. Hence, it is submitted that petitioner is liable to the two and one-half percent (2.5%) Gross Philippine Billings Tax under Section 28 (A)(3)(b) of the Tax Code, as amended.
>
> 8. Assuming *arguendo* that petitioner is not liable for the Gross Philippine Billings Tax as provided for in Section 28(A)(3)(b) of the Code, sales revenues derived for the freight and cargo loaded in the Philippines by the petitioner, a non-resident foreign corporation organized and existing under the laws of Denmark, in the year 2001 is **subject to the 32% Final**

[6] Docket, pp. 1 -10.

Gross Income Tax under **Section 28(B)(1)** of the Tax Code, as amended. It provides that:

> 'Section 28. Rates of Income Tax on Foreign Corporations. –
>
> (A) Tax on Resident Foreign Corporations. –
> (B) Tax on Non-Resident Foreign Corporation. -
>
> (1) In General. – Except as otherwise provided in this Code, a foreign corporation not engaged in trade or business in the Philippines shall pay a tax equal to thirty-five percent (35%) of the **gross income received during each taxable year from all sources within the Philippines**, xxx and effective January 1, 2000 and thereafter, the rate shall be thirty-two percent (**32%**).' (emphasis supplied)

Hence, in the case at bar, assuming *arguendo* that petitioner is not liable for the Gross Philippine Billings Tax provided for in Section 28 (A)(3)(b) of the Code, it is submitted that petitioner, **as a non-resident foreign corporation**, is liable for a higher income tax rate of 32% under **Section 28(B)(1)** of the Tax Code, as amended.

In any case, the petitioner is not entitled to any tax refund but may even be held liable for a deficiency income tax for the difference between the 32% and the 2½% tax rates as previously discussed.

9. Assuming but without admitting that the RP-Kingdom of Denmark Tax Treaty applies to the instant case, the same must be proven as a fact.

10. Assuming further but without admitting that the 'most favored nation clause' applies to the instant case, the same must be proven as a fact.

11. Taxes paid and collected by the BIR are presumed to have been made in accordance with law, and the burden of proof to prove otherwise is upon the petitioner.

12. To support its claim, it is imperative for petitioner to prove that the petitioner's administrative and judicial claims for tax refund of the alleged erroneously paid tax on Gross Philippine Billings for the taxable year 2001 was filed within

two (2) years from the date of the payment of the tax regardless of any supervening cause that may arise after payment in accordance with Sections 204(C) and 229 of the Tax Code, as amended.

13. Furthermore, in an action for refund the burden of proof is on the taxpayer to establish its right to refund and failure to sustain the burden is fatal to the claim for refund/credit. This is so because exemptions from taxation are highly disfavored in law and he who claims exemptions must be able to justify his claim by the clearest grant of organic or statutory law. An exemption from common burden cannot be permitted to exist upon vague implications. (*Asiatic Petroleum Co. [P.I.] v. Llanes, 49 Phil. 466* cited in *Collector of Internal Revenue v. Manila Jockey Club, Inc. 98 Phil. 670*).

14. Claims for refund are construed strictly against the claimant for the same partake the nature of exemption from taxation.[7]"

THE ISSUES

The parties jointly stipulated the following issues for the consideration of this Court:

"1. Whether or not petitioner has complied with the provisions of Sections 204(C) and 229 of the 1997 Tax Code on the prescriptive period for filing administrative and judicial claims for tax refund;

2. Whether or not A.P. Moller-Maersk A/S's Gross Philippine Billings is subject to tax at the rate of 2.5% pursuant to Section 28(A)(3) of the Tax Code;

3. Assuming *arguendo* that A.P. Moller-Maersk A/S is not liable for the 2.5% Gross Philippine Billings' tax, whether or not A.P. Moller-Maersk A/S, as a non-resident foreign corporation, is liable for a higher income tax rate of 32% under Section 28(B)(1) of the 1997 Tax Code;

4. Whether or not petitioner is the general shipping agent of A.P. Moller-Maersk A/S in the Philippines;

5. Whether or not A.P. Moller-Maersk A/S owns and operates vessels traversing the high seas to load cargoes from, and transport and deliver the same to, different international seaports including the Philippines;

[7] Docket, pp. 148-153.

6. Whether or not A.P. Moller-Maersk A/S had authorized Maersk Filipinas Inc. to file the petition for review before this Court covering the subject matter of this case;

7. Whether or not sales revenues covering the taxable year 2001 of A.P. Moller-Maersk A/S for freight and cargo allegedly loaded in the Philippines by its international vessels were remitted to it after the same were subjected to Philippine income taxation within the reglementary period provided by law, rules and regulations;

8. Whether or not during the taxable year 2001, A.P. Moller-Maersk A/S generated a total gross sales of P4,285,629,494.00;

9. Whether or not A.P. Moller-Maersk A/S filed its Income Tax Return for the taxable year 2001;

10. Whether or not the alleged annual gross sales of A.P. Moller-Maersk is a consolidation and cumulative of its quarterly sales;

11. Whether or not the ticket sales of the international vessels of A.P. Moller-Maersk for the transport of cargo from the Philippines to foreign international ports is exempt from income taxation;

12. Whether or not the most favored nation clause under the Philippines-Denmark Tax Treaty applies in the instant case;

13. Whether or not petitioner is entitled to a refund in the amount of P64,284,442.42;

14. Assuming *arguendo* that petitioner is entitled to refund, whether or not petitioner is the proper party that may claim for refund. [8]"

We summarize the foregoing issues raised by both parties as follows:

1. Whether or not petitioner has complied with the provisions of Sections 204(C) and 229 of the 1997 Tax Code on the prescriptive period for filing administrative and judicial claims for tax refund;

2. Whether or not A.P. Moller-Maersk A/S owns and operates vessels traversing the high seas to load cargoes

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[8] Joint Stipulation of Facts and Issues, Docket, pp. 173-176.

from, and transport and deliver the same to, different international seaports including the Philippines;

3. Whether or not petitioner is the general shipping agent of A.P. Moller-Maersk A/S; and whether or not A.P. Moller-Maersk A/S had authorized herein petitioner, Maersk Filipinas Inc., to file the petition for review before this Court covering the subject matter of this case;

4. Whether or not petitioner is the proper party to claim the refund of the alleged erroneous income tax payments; and

5. Whether or not A.P. Moller-Maersk A/S, a resident of the Kingdom of Denmark, is entitled to the "most favored nation clause" under Article 8(2)(b) of the RP-Denmark Tax Treaty, in relation to Article 12(1) of the Agreement Between the Government of the Republic of the Philippines and the Government of the Republic of Cyprus on Merchant Shipping.

6. Whether or not petitioner is entitled to a refund in the amount of P64,284,442.42.

THE COURT'S RULING

The first, second, third and fourth issues are resolved in the affirmative.

The two-year prescriptive period for the filing of a claim for refund commences from the date of filing of the final adjustment return.[9] The alleged erroneous income tax payments on the Gross Philippine Billings subject of the instant petition involves the taxable year 2001, for which Petitioner filed its Original Annual Income Tax Return on April 16, 2002[10]. Counting from this date, petitioner's administrative and judicial claims for refund filed on April 5, 2004 and April 13, 2004, respectively, fall within the two-year period prescribed under Section 204(C) in relation to Section 229 of the National Internal Revenue Code (NIRC) of 1997.

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[9] ACCRA Investments Corporation vs. Court of Appeals, 204 SCRA 957.
[10] Exhibit "S".

As regards the second, third and fourth issues, petitioner presented in evidence the following documents to prove the nature of business conducted by A.P. Moller-Maersk A/S and its agency agreement with Maersk Filipinas, Inc., to wit:

1. Copy of the Agency Agreement commencing from January 1, 1997 entered into by and between herein petitioner and A.P. Moller, acting as the Managing Owner of Aktieselskabet Dampskibsselskabet Svendborg and Dampskibsselskabet AF 1912, Aktieselskab, duly authenticated by the Vice-Consul of the Consulate General of the Philippines in Copenhagen, Denmark;

2. Copies of the translated Official Declaration from the Danish Commerce and Companies Agency[11] declaring the merger between Dampskibsselskabet AF 1912, Aktieselskab and Aktieselskabet Dampskibsselskabet Svendborg, both dated June 16, 2003, duly authenticated by the Vice-Consul of the Consulate General of the Philippines in Copenhagen, Denmark;

3. Copy of the translated Articles of Association of A.P. Moller-Maersk A/S[12], duly authenticated by the Vice-Consul of the Consulate General of the Philippines in Copenhagen, Denmark;

4. Original copy of the Sworn Affidavits of Mr. Edwin Marasigan dated April 13, 2005, September 12, 2005, and January 17, 2007;

5. Faithful reproduction of the original Bills of Lading;

6. Faithful reproduction of the original Certificate of BIR Registration of A.P. Moller-Maersk A/S dated May 23, 2003[13]; and

7. Faithful reproduction of the original Certificate of BIR Registration of Maersk-Filipinas, Inc. dated June 30, 1996[14].

[11] Exhibits "C" and "D".
[12] Exhibit "E".
[13] Exhibit "Z"-"Z-3".
[14] Exhibit "AA"-"AA3".

Based on the documents presented, it is apparent that A.P. Moller-Maersk A/S, Dampskibsselskabet AF 1912, Aktieselskab, and Aktieselskabet Dampskibsselskabet Svendborg are Danish registered entities engaged in the shipping and chartering business. All companies have as their managing owner the Firm of A.P. Moller. Thereafter, Aktieselskabet Dampskibsselskabet Svendborg merged with Dampskibsselskabet AF 1912, Aktieselskab, with the former entity as the surviving company, as confirmed by the Danish Commerce and Companies Agency in an Official Declaration dated June 16, 2003. [15] In connection with the said merger, Aktieselskabet Dampskibsselskabet Svendborg changed its name to A.P. Moller-Maersk A/S. On June 12, 2003, the Articles of Association of A.P. Moller-Maersk A/S was adopted.

Whenever a merger between two corporations occurs, and as provided under the National Internal Revenue Code of 1997, one corporation acquires all or substantially all the properties of another corporation[16]. Effectively therefore, when Aktieselskabet Dampskibsselskabet Svendborg merged with Dampskibsselskabet AF 1912, Aktieselskab, and subsequently, changed its surviving name to A.P. Moller-Maersk A/S, the latter then absorbed all or substantially all the properties of the merged corporations. Such purpose and consequence can be seen from the provision of the Articles of Association of A.P. Moller-Maersk A/S which states that "*the company will also trade under the following business names: Aktieselskabet Dampskibsselskabet*

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[15] Exhibits "C" and "D".
[16] Sec.40 (C) (6)(b), NIRC of 1997.

Svendborg (A.P. Moller-Maersk A/S) and Dampskibsselskabet af 1912, Aktieselskab (A.P. Moller-Maersk A/S) [17]*."*

To prove the right of petitioner Maersk Filipinas, Inc. to file the instant petition for and on behalf of A.P. Moller-Maersk A/S, as the latter's duly designated general shipping agent here in the Philippines, petitioner submitted the Agency Agreement[18] entered into with the latter. It may be that the Agency Agreement was signed for by A.P. Moller; however, it cannot be overly emphasized that A.P. Moller is the managing owner of A.P. Moller-Maersk A/S. As the managing owner, it has been given the power to represent the company in all matters and shall exercise any authority generally vested in a managing owner, effectively binding the company, A.P. Moller-Maersk A/S, in its own name.[19]

With respect to respondent's insistence that petitioner has no legal personality to institute the instant Petition for Review inasmuch as petitioner was allegedly registered with the BIR only on May 23, 2002 while the subject matter of the refund pertains to the taxable year 2001, records reveal that petitioner was registered with the Bureau of Internal Revenue on June 30, 1996, as evidenced by its Certificate of Registration[20] filed with the office of respondent. It became the General Agent of all of A.P. Moller's activities, including those of Aktieselskabet Dampskibsselskabet Svendborg (A.P. Moller-Maersk A/S), Dampskibsselskabet af 1912, Aktieselskab, and A.P. Moller-Maersk A/S, pursuant to the Agency Agreement executed by the

[17] Exhibit "E".
[18] Exhibit "T".
[19] Exhibit "E".
[20] Exhibit "AA", Petitioner's Rebuttal Evidence, Docket, p. 348.

parties on January 1, 1997. Clearly, the instant Petition was filed by petitioner **"for and in behalf of A.P. Moller-Maersk A/S"**. It is elementary in law that when an agent acts for and in behalf of a principal, the principal's name must likewise be shown. Indubitably, petitioner has complied with this mandate.

Anent petitioner's assertion that the Gross Philippine Billings of A.P. Moller-Maersk A/S for the taxable year 2001 is a consolidation and cumulative of its quarterly sales reported in the quarterly income tax returns and annual income tax return (Exhibits "J", "L", "N" and "S") filed by petitioner on behalf of AP Moller on May 29, 2001, August 28, 2001, November 21, 2001 and April 16, 2002, respectively in the total amount of P4,285,629,494.00, We find the same to be well-founded. A close scrutiny of petitioner's Quarterly[21] and Annual[22] Income Tax Return filed for the taxable year 2001, shows that A.P. Moller-Maersk A/S indeed generated a total gross sales of P4,285,629,494.00 and the corresponding income taxes equivalent to 1.5% of its gross sales for the same year were remitted and paid by petitioner on behalf of A.P. Moller-Maersk A/S.

Going now to the fifth and sixth issues, petitioner argues that it had erroneously and improperly withheld and remitted its principal's income taxes on the Gross Philippine Billings at 1.5% tax rate, invoking the provision on the "most favored nation clause" under Article 8, Section 2(b) of the RP-Denmark Tax Treaty in relation to Article 12(1) of the Agreement Between the Government of the Republic of the Philippines and the Government of the Republic of Cyprus on Merchant Shipping. According to petitioner, residents

[21] Exhibits "J", "L", and "N".
[22] Exhibit "S".

of the Republic of Cyprus are exempt from the payment of Philippine income taxes under Article 12(1) of the "***Agreement between the Government of the Republic of the Philippines and the Government of the Republic of Cyprus on Merchant Shipping*"**. Thus, petitioner seeks beneficial coverage under the "most favored nation clause" mentioned under the RP-Denmark Tax Treaty, and thereby insists that its profits from its shipping operation in the Philippines should also not be taxable considering the exemption enjoyed by residents of the Republic of Cyprus engaged in merchant shipping.

We disagree.

The "most favored nation clause" has for its purpose the granting to a contracting state treatment not less favorable than that which has been or may be extended to the "most favored" among other countries. It has been the intention of the phrase to establish the principle of equality among residents and enterprises of contracting states. In applying the doctrine or principle of the "most favored nation clause", the Supreme Court in the case of **Commissioner of Internal Revenue vs. S.C. Johnson & Son, Inc.** (S.C. Johnson Case) laid down the condition precedent for its entitlement, thus:

> "As stated earlier, the ultimate reason for avoiding double taxation is to encourage foreign investors to invest in the Philippines — a crucial economic goal for developing countries. The goal of double taxation conventions would be thwarted if such treaties did not provide for effective measures to minimize, if not completely eliminate, the tax burden laid upon the income or capital of the investor. Thus, if the rates of tax are lowered by the state of source, in this case, by the Philippines, there should be a concomitant commitment on the part of the state of residence to grant some form of tax relief, whether this be in the form of a tax credit or exemption. Otherwise, the tax which could have been collected by the Philippine government will simply be collected by another state, defeating the object of the tax treaty since the tax burden imposed upon the investor would remain unrelieved. If the state of residence does not grant some form of

tax relief to the investor, no benefit would redound to the Philippines, i,e., increased investment resulting from a favorable tax regime, should it impose a lower tax rate on the royalty earnings of the investor, and it would be better to impose the regular rate rather than lose much-needed revenues to another country.

At the same time, the intention behind the adoption of the provision on 'relief from double taxation' in the two tax treaties in question should be considered in light of the purpose behind the most favored nation clause.

The purpose of a most favored nation clause is to grant to the contracting party treatment not less favorable than that which has been or may be granted to the 'most favored' among other countries. The most favored nation clause is intended to establish the principle of equality of international treatment by providing that the citizens or subjects of the contracting nations may enjoy the privileges accorded by either party to those of the most favored nation. The essence of the principle is to allow the taxpayer in one state to avail of more liberal provisions granted in another tax treaty to which the country of residence of such taxpayer is also a party **provided that the subject matter of taxation, in this case royalty income, is the same as that in the tax treaty under which the taxpayer is liable.** Both Article 13 of the RP-US Tax Treaty and Article 12 (2) (b) of the RP-West Germany Tax Treaty, above-quoted, speaks of tax on royalties for the use of trademark, patent, and technology. The entitlement of the 10% rate by U.S. firms despite the absence of a matching credit (20% for royalties) would derogate from the design behind the most favored nation clause to grant equality of international treatment since the tax burden laid upon the income of the investor is not the same in the two countries. **The similarity in the circumstances of payment of taxes is a condition for the enjoyment of most favored nation treatment precisely to underscore the need for equality of treatment**.

We accordingly agree with petitioner that since the RP-US Tax Treaty does not give a matching tax credit of 20 percent for the taxes paid to the Philippines on royalties as allowed under the RP-West Germany Tax Treaty, private respondent cannot be deemed entitled to the 10 percent rate granted under the latter treaty for the reason that there is no payment of taxes on royalties under similar circumstances.[23]"

[23] G.R. No. 127105, June 25, 1999, 309 SCRA 87, at pp. 107-108, emphasis supplied.

In the aforequoted case, the Supreme Court interpreted the phrase "paid under similar circumstances" under the “most favored nation clause” of the RP-US Tax Treaty as referring to the payment of taxes and not royalties. The Supreme Court did not allow the application of the lower rate of 10% under the RP-Germany Tax Treaty for royalties paid to US residents because the RP-US Tax Treaty contains no "**matching credit**" provision similar to that found in Article 24 of the RP-Germany Tax Treaty. Notably, in order that a taxpayer in one state may avail of more liberal provisions granted in another state’s tax treaty, and the country of residence of such taxpayer is also a state party to the said tax treaty, it is a pre-requisite that the subject matter be the same as that in the tax treaty under which the taxpayer is liable.

We therefore find the necessity to make a careful comparison between the *RP-Denmark Tax Treaty* and the *RP-Cyprus Agreement on Merchant Shipping.* From the very titles of said documents, it appears that the former is a treaty pertaining to taxation, while the latter is an agreement pertaining to merchant shipping. A “treaty” is defined as an agreement between the States, including international organizations of States, intended to create legal rights and obligations of the parties thereto.[24] On the other hand, an “Agreement” usually denotes an instrument of a more limited scope or lesser importance than either a treaty or a convention. It frequently relates to administrative and technical matters and is generally not subject to ratification.[25]

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[24] Report on the Law of Treaties, H. Lunterpacht, Special Rapporteur, for the fifth session of the International Law Commission (1953), U.N. Doc., A/CN, 4/63, Cf.
[25] Public International Law, Salonga & Yap, 2nd Edition, 1963.

In the same **S.C. Johnson case**,[26] the Supreme Court elaborated on the nature and purpose of a tax treaty (which includes the subject *RP-Denmark Tax Treaty),* to wit:

> "The RP-US Tax Treaty is just one of a number of bilateral treaties which the Philippines has entered into for the avoidance of double taxation. The purpose of these international agreements is to reconcile the national fiscal legislations of the contracting parties in order to help the taxpayer avoid simultaneous taxation in two different jurisdictions. More precisely, the tax conventions are drafted with a view towards the elimination of international juridical double taxation, which is defined as the imposition of comparable taxes in two or more states on the same taxpayer in respect of the same subject matter and for identical periods. The apparent rationale for doing away with double taxation is to encourage the free flow of goods and services and the movement of capital, technology and persons between countries, conditions deemed vital in creating robust and dynamic economies. Foreign investments will only thrive in a fairly predictable and reasonable international investment climate and the protection against double taxation is crucial in creating such a climate.
>
> Double taxation usually takes place when a person is resident of a contracting state and derives from, or owns capital in, the other contracting state and both states impose tax on that income or capital. In order to eliminate double taxation, a tax treaty resorts to several methods. First, it sets out the respective rights to tax of the state of source or situs and of the state of residence with regard to certain classes of income or capital. In some cases, an exclusive right to tax is conferred on one of the contracting states; however, for other items or income or capital, both states are given the right to tax, although the amount of tax that may be imposed by the state of source is limited."

Looking now at the *RP-Denmark Tax Treaty* and *the RP-Cyprus Agreement* on Merchant Shipping, it appears said treaty and agreement do not have similar provisions on taxation, as well as on the manner of tax payment. The *RP-Denmark Tax Treaty*, signed on December 16, 1966 and became effective on January 1, 1974, and subsequently renegotiated on

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[26] *Supra.*

January 1, 1998, was entered into by the Republic of the Philippines and the Kingdom of Denmark with the purpose of concluding a Convention for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income.

On the other hand, the *RP-Cyprus Agreement on Merchant Shipping* is the agreement between the Government of the Republic of the Philippines and the Government of the Republic of Cyprus on the field of merchant shipping. Paragraph 1 of the Agreement states that:

> "The Government of the Republic of the Philippines, and the Government of the Republic of Cyprus hereinafter referred to as the 'Contracting Parties',
>
> Desiring to strengthen the friendly relations between the two countries and to intensify their economic relations;
>
> Aiming to develop and promote cooperation between the Republic of the Philippines and the Republic of Cyprus in the field of merchant shipping on a mutually advantageous position in accordance with their respective needs and objectives for economic development;
>
> Hence agreed as follows:
>
> **ARTICLE I**
>
> The Contracting Parties agree to cooperate on the basis of equal rights, mutual benefit and the principle of freedom of merchant shipping in order to develop the relations between the Republic of the Philippines and the Republic of Cyprus in the field of merchant shipping."

It can be gleaned from the aforequoted provisions that the *RP-Cyprus Shipping Agreement* refers to a maritime agreement entered into, by the Philippines and the Republic of Cyprus, for the purpose of strengthening and intensifying friendly and economic relations between the two contracting states. It was also executed to develop and promote cooperation between the Philippines and Cyprus in the field of merchant shipping, on a mutually advantageous basis in accordance with their respective needs and objectives for economic development. Thus, there appears to be no similarity in the subject matter of subject documents. In fact, these Agreements relate to two different issues and fields. We illustrate, as follows:

Article 8 of the *RP-Denmark Tax Treaty* reads:

RP-Denmark Tax Treaty

Article 8
Shipping and Air Transport

1. Profits derived by an enterprise which has its place of effective management in a Contracting State from the operation in international traffic of ships or aircraft may be taxed in that State.

2. Notwithstanding the provisions of paragraph 1, profits from sources within the Contracting State derived by an enterprise of the other Contracting State from the operation of ships or aircraft in international traffic may be taxed in the first mentioned State but, the tax so charged shall not exceed the lesser of:

    a.) one and one-half percent of the gross revenues derived from sources in that State; and

    b.) the lowest rate that may be imposed on profits of the same kind derived under similar circumstances by a resident of a third State.

On the other hand, Article 12 of the *RP-Cyprus Agreement on Merchant Shipping* states that:

RP-Cyprus Agreement on Merchant Shipping

Article 12

1. Profits from the operation of a shipping enterprise, registered under the laws and regulations of either of the Contracting Parties, in international traffic, including profits derived from its participation in a pool, a joint business or in an international operation agency, shall be

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taxable only in the Contracting Party where the registered office of the enterprise is situated.

2. Earnings of seamen or seafarers who are citizens of either Contracting Party shall be taxed in accordance with the national laws of the Contracting Parties."

From the afore-quoted provisions, it is thus clear that Article 8 of the *RP-Denmark Tax Treaty* pertains to "Shipping and Air Transport"; while Article 12 of the *RP-Cyprus Agreement on Merchant Shippin*g concerns "Merchant Shipping". Evidently, the condition precedent before the provision on the "most favored nation clause" may be invoked, as explained in the **S.C. Johnson Case** [27], is wanting in this case. Consequently, petitioner cannot invoke what is clearly not applicable to its case.

It is a cardinal rule in taxation that laws granting tax exemption are construed *strictissimi juris* against the taxpayer and liberally in favor of the taxing authority. The tax exemption cannot arise by mere implication and any doubt whether the exemption exists is strictly construed against the taxpayer and in favor of the taxing authority. The burden of proof is upon him who claims the exemption in his favor and he must be able to justify his claim by the clearest grant of organic or statute law.[28]

It must be made clear that an exemption from taxation cannot be allowed unless granted in the most explicit and categorical language and must be strictly construed against the taxpayer.[29] In this case, it is evident that petitioner is not a tax-exempt corporation; therefore, to claim that it cannot be held liable to pay its income taxes, is clearly unmerited.

[27] *Supra.*
[28] Wonder Mechanical Engineering Corp. vs. CTA, 64 SCRA 555.
[29] Insular Lumber Co. vs. Court of Tax Appeals, 104 SCRA 710.

Inasmuch as there is no legal basis for petitioner's claim for tax refund or issuance of a tax credit, the Court is left with no other recourse but to deny the instant petition.

WHEREFORE, the present Petition for Review is hereby **DISMISSED** for lack of merit.

SO ORDERED.

ERLINDA P. UY
Associate Justice

WE CONCUR:

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.
Associate Justice
Chairperson

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