REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

BRITISH OVERSEAS AIRWAYS CORPORATION,
Petitioner,

- versus -

C.T.A. CASE NO. 2373

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

x - - - - - - - - - - - - x

BRITISH OVERSEAS AIRWAYS CORPORATION,
Petitioner,

- versus -

C.T.A. CASE NO. 2561

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

x - - - - - - - - - - - - x

1/26/83

D E C I S I O N

British Overseas Airways Corporation, petitioner in these two cases, poses the question before us of whether the revenue derived by it from the sales of passage tickets in the Philippines for international air transportation service is income derived from sources within the Philippines subject to Philippine income tax.

Petitioner British Overseas Airways Corporation (BOAC for short) asserts that its revenue from the sales of tickets in the Philippines is considered income from sources outside the Philippines because it is not the activity of selling tickets that produced the income sought to be taxed but the service of transportation which was rendered outside the Philippines. As the source of income is the place where the service is rendered, it follows that the income was derived from sources outside the Philippines and therefore not taxable under Philippine income tax law.

In brushing aside this stand of petitioner, respondent Commissioner of Internal Revenue, after alleging in his answers to the petitions for review that BOAC was engaged in business in the Philippines and derived income from sources within the country, avers that the revenue derived by BOAC from the sales of tickets in the Philippines for international air transportation service is income derived from sources partly within and partly without the Philippines contemplated under Section 37(e) in relation to Section 24(b) of the National Internal Revenue Code. Pursuant to Section 152 of Revenue Regulations No. 2, otherwise known as the Income Tax Regulations, income from sources within the Philippines subject to Philippine income tax includes that derived in full from sources within the Philippines and that portion of the income derived partly from sources within and partly from sources without the Philippines which is allocated or apportioned to sources within the Philippines.

There is no controversy as to the facts of these cases. As narrated by petitioner in his memorandum dated January 7, 1981 (pp. 164-169, CTA records) and adopted by respondent in his statement of facts in his supporting memorandum (p. 217, id.):

> CTA CASE NO. 2373
>
> Petitioner British Overseas Airways Corporation (hereinafter called BOAC), is a foreign corporation organized and existing under the laws of the United Kingdom, a member of the International Air Transport Association (IATA) without, prior to April, 1980, any landing rights for traffic purposes in the Philippines. On 7 May 1968, petitioner was served with an assessment letter dated 1 April 1968 of Respondent Commissioner (hereinafter also called Commissioner, for short) covering deficiency income taxes for the years 1959 to 1963 in the aggregate amount of ₱2,498,358.56 (Exh. "A"); but Petitioner, having known said assessment even prior to the receipt of notice thereof, had already filed through its lawyers with Respondent a letter dated 6 May 1968 protesting the assessment (Exh. "B"). This letter was followed by another letter dated 10 May 1968 protesting and requesting for a reconsideration of the assessment (Exh. "C"). Respondent issued, following a further investigation of the matter, a new assessment for the years 1959 to 1967 per his letter dated 16 January 1970 (Exh. "D") superseding the assessment contained in the letter dated 1 April 1968, as a

consequence of which petitioner was compelled to pay on 28 January 1970 the new assessment aggregating ₱858,307.79 under the following official receipts:

Official Receipt No.	Amount	
4100109	₱157,452.71	(Exh. "E")
4100110	206,767.69	(Exh. "E-1")
4100111	600.00	(Exh. "E-2")
4100112	139,814.10	(Exh. "E-3")
4100113	276,721.60	(Exh. "E-4")
4100114	18,113.51	(Exh. "E-5")
4100115	12,206.18	(Exh. "E-6")
4100116	46,632.00	(Exh. "E-7")
TOTAL	₱858,307.79	

Petitioner filed on 7 October 1970 with Respondent a claim for refund of ₱858,307.79 pursuant to Sec. 306 of the National Internal Revenue Code (Exh."F"). Inasmuch as Petitioner did not receive acknowledgment of the receipt of said letter or the refund requested, Petitioner reiterated in a letter dated 25 November 1971 its request for refund and asked for cancellation of the assessment for 1969-1971 (Exh. "G"). Respondent, in its letter dated 8 December 1971, stated that it finally realized, after reinvestigation of the case, that Petitioner is not subject to payment of Philippine income tax (Exh. "H"), but notwithstanding said ruling, Respondent failed to finalize petitioner's request for refund. Hence, Petitioner filed the present petition docketed as CTA Case No. 2373, alleging the abovestated facts and praying that this Honorable Court declare illegal the collection of the amount of ₱858,307.79 and order the said amount refunded.

In his answer, Respondent admitted almost all the material allegations of the complaint, but alleged that the letter dated 6 December 1970 had been revoked. Respondent further denied that Petitioner was compelled to pay the deficiency income tax of ₱858,307.79 and that the collection of said tax was illegal. As defenses, Respondent alleged that Petitioner was engaged in business in the Philippines, derived income from the Philippines, and is subject to income tax, and the income tax sought to be refunded was imposed on income received from sources within the Philippines.

The parties submitted a "Partial Stipulation of Facts" dated 10 November 1975 wherein the parties admitted, among others, that Petitioner is being a foreign corporation organized and existing under the laws of the United Kingdom and the documentary evidence contained in the pleadings, Annexes "A", "B", "C", "D", "E", "E-1" to "E-7", "F", "G", and "H" to the petition; that Petitioner is engaged in the international airline business, a member of the IATA, without landing rights for traffic purposes in the Philippines and, consequently, did not (until April, 1980) carry passengers and/or to and from the Philippines for it was not during the period in question granted by the Civil Aeronautics Board (CAB) a certificate of public convenience and necessity to operate in the Philippines, and is, as such, an off-line carrier under Revenue Regulations Nos. 6-66 dated 1 December 1966; that Petitioner, during the period covered by the assessment, maintained a general sales agent in the Philippines which was responsible for selling BOAC tickets covering passengers and cargoes.

<u>CTA CASE NO. 2561</u>

Petitioner British Overseas Airways Corporation (BOAC for brevity) is a 100% British government-owned corporation, created and existing under the laws of the United Kingdom. It is a member of the International Air Transport Association (IATA); engaged in international airline business, but had no landing rights for traffic purposes in the Philippines (until only in April, 1980) and, consequently, did not carry passengers and/or cargo to or from the Philippines. On or about 25 November 1971, it was served with an assessment letter from Respondent Commissioner of Internal Revenue (hereinafter also referred to as Commissioner, for brevity) dated 17 November 1971 covering deficiency income taxes including interests and penalty allegedly due from BOAC for the fiscal year ended 31 March 1969 through 31 March 1971 inclusive in the aggregate amount of ₱549,327.43 and demanding an additional ₱1,000.00 as compromise penalty for violation of Sec. 74 of the National Internal Revenue Code (Exh. "A"). On 25 November 1971, Petitioner wrote Respondent a letter requesting a ruling that, for reasons stated therein, the Petitioner be held not liable to Philippine income tax and that the assessment be countermanded or set aside (Exh. "B"). On 13 December 1971, Petitioner received through counsel a letter dated 8 December 1971 from Respondent stating that, "after reinvestigation of the case and a careful analysis of the facts and the law involved therein, respondent's Office has finally decided that your client (Petitioner) is not subject to the payment of Philippine income tax" and that the assessments dated 17 November 1971 were withdrawn and cancelled (Exh. "C"). Petitioner, through counsel, received later a letter dated 16 February 1972 from Respondent wherein Respondent denied Petitioner's previous request for tax refund for certain years prior to the fiscal year 1968/69 and also issued new income tax assessments for the fiscal years ended 31 March 1969 through 31 March 1971 inclusive, in the aggregate amount of ₱534,132.08 (Exh. "D"). Petitioner in its letter dated 23 March 1972 requested Respondent to reconsider its action in issuing the assessments for deficiency income taxes for the fiscal year ended March 31, 1969 through March 31, 1971 and to defer the action on the refund of the taxes paid by Petitioner for prior years until this Court shall have decided the same issue of Petitioner's liability for income tax in CTA Case No. 2373 (Exh. "E"). Petitioner again wrote Respondent on 17 August 1972 supplementing its arguments on the non-liability of Petitioner for Philippine income tax (Exh. "F"). Under date of 15 December 1972, Petitioner through counsel inquired from Respondent the status of its request for reconsideration (Exh. "G"). On 27 September 1973, Petitioner received through counsel, a letter dated 24 August 1973 from Respondent denying Petitioner's request for reconsideration and reiterating the demand for payment contained in the letter dated 16 February 1972 (Exh. "H"). Hence, Petitioner filed its petition for review dated 10 October 1973, docketed as CTA Case No. 2561 alleging the above facts and praying that this Honorable Court render judgment to the effect that Petitioner is not liable for Philippine income tax.

Respondent in his answer dated 29 January 1974 denied that Petitioner does not carry passengers or cargo to and from the Philippines and that Petitioner is not subject to Philippine income tax; and alleged as defenses that Petitioner is engaged in business in the Philippines and derives income from Philippine sources for which it is liable to payment of income tax.

Petitioner and Respondent submitted in May, 1976 a "Partial Stipulation of Facts" wherein the parties admitted: the documentary evidence (Annexes "A", "A-1" to "A-3", "B", "C", "D", "D-1" to "D-3", "E", "F", "G", and "H" to the Petition); that Petitioner is engaged in international airline service, a member of the IATA, and during the period covered

by the questioned assessment had no landing rights for traffic purposes in the Philippines, except for a nine-month period, partly in 1961 and partly in 1962, when it was granted a temporary landing permit and that, consequently, Petitioner did not carry passengers and/or cargo to and from the Philippines as it was never granted by the Civil Aeronautics Board (CAB) a certificate of public convenience and necessity to operate in the Philippines; that Petitioner is considered an off-line carrier under Revenue Regulations No. 6-66 dated 1 December 1966; and that Petitioner, during the period covered by the assessment, maintained a general sales agent in the Philippines which was responsible for selling in its own name BOAC tickets for air transport of passenger and cargoes to and from foreign cities.
The two (2) cases were tried jointly.

Inasmuch as the two appeals raise the same issue, they are consolidated also in this Decision.

In raising the question of the taxability of the revenue derived by petitioner from the sales of tickets in the Philippines for international air transportation service through its general sales agent, the Warner Barnes & Co., Ltd., and later by the Qantas Airways, respondent alleges as special and affirmative defenses in his answers to the petitions for review that:

(a) During the period in question, petitioner was engaged in business in the Philippines and derived income from sources within the Philippines;

(b) Petitioner is a resident foreign corporation liable to income tax on income from all sources within the Philippines (Sec. 24(b)(2), National Internal Revenue Code);

(c) In the alternative that petitioner may not be considered a resident foreign corporation but a non-resident foreign corporation, then it is liable to Philippine income tax at the rate of thirty-five percent (35%) of its gross income received from all sources within the Philippines (Sec. 24(b)(1), National Internal Revenue Code).

For purposes of income taxation, the taxability of foreign corporations at the time material to this case, whether engaged in trade or business in the Philippines or not engaged in trade or business here depends on whether the income is derived from sources within the Philippines. (Sec. 24, National Internal Revenue Code; Secs. 16 & 60, Rev. Reg. No. 2) While a foreign corporation doing business in the Philippines is taxable on income solely from sources within the Philippines, it is permitted to claim deductions from gross income but only to the extent connected with income earned in the Philippines. (Secs. 24(b)(2) and 37, National Internal Revenue Code.) On the other hand, a foreign corporation not doing business in the Philippines is taxable on income "from all sources within the Philippines, as interest, dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, or other fixed or determinable annual or periodical or casual gains, profits and income and capital gains." (Sec. 24(b)(1), National Internal Revenue Code.)

The decisive question, therefore, is whether or not the proceeds of sales in the Philippines of BOAC passage tickets by the Warner Barnes & Co., Ltd., and later by the Qantas Airways during the period in question, and on which the assessments involved herein were based, constitute income of petitioner from Philippine sources.

The controlling statute is Section 37 of the National Internal Revenue Code, the pertinent portions of which during the years in question, reads as follows:

> SEC. 37. Income from sources within the Philippines - (a) Gross income from sources within the Philippines. - The following items of gross income shall be treated as gross income from sources within the Philippines:

(1) Interest.- Interest derived from sources within the Philippines, and interest on bonds, notes, or other interest-bearing obligations of residents, corporate or otherwise;

(2) Dividends.- The amount received as dividends

(A) From a domestic corporation;

(B) From a foreign corporation unless less than fifty per centum of the gross income of such foreign corporation for the three-year period ending with the close of its taxable year preceding the declaration of such dividends (or for such part of such period as the corporation has been in existence) was derived from sources within the Philippines as determined under the provisions of this section; but only in an amount which bears the same ratio to such dividends as the gross income of the corporation for such period derived from sources within the Philippines bears to its gross income from all sources;

(3) Services.- Compensation for labor or personal services performed in the Philippines;

(4) Rentals and royalties.- Rentals and royalties from property located in the Philippines or from any interest in such property, including rentals or royalties for the use of or for the privilege of using in the Philippines patents, copyrights, secret processes and formulas, goodwill, trademarks, trade brands, franchise, and other like property;

(5) Sale of real property.- Gains profits, and income from the sale of real property located in the Philippines; and

> (6) Sale of personal property.- Gains, profits, and income from the sale of personal property, as determined in subsection (e) of this section.
>
> (b) Net income from sources in the Philippines.- From the items of gross income specified in subsection (a) of this section there shall be deducted the expenses, losses, and other deductions properly apportioned or allocated thereto and a ratable part of any expenses, losses, or other deductions which cannot definitely be allocated to some item or class of gross income. The remainder, if any, shall be included in full as net income from sources within the Philippines.

Adverting to the terms of the law, it is quite apparent that the proceeds of sales of BOAC passage tickets in the Philippines by the Warner Barnes & Co., Ltd., and later by the Qantas Airways during the period in question could not be considered as interest, dividends or rentals and royalties derived from sources within the Philippines. There is patently an absence of analogy or similarity between interest, dividends, rentals or royalties and proceeds of sales of airline passage tickets. And by no stretch of the imagination could such proceeds of sales of airline passage tickets be compared to income "from the sale of personal property produced (in whole or in part)" by petitioner and sold within the Philippines so as to be treated as income derived partly from sources within and partly from sources without the Philippines under Section 37(e) of the then in force National Internal Revenue Code. (Japan Air Lines, Inc. vs. Commissioner of Internal Revenue, CTA Case No. 2480, January 15, 1982.)

It seems already settled that such proceeds of sales of airline passage tickets in the Philippines of an international air carrier of passengers and/or freight are considered "compensation for labor or personal services performed in the Philippines", if the service of transportation is performed in the Philippines; that is, compensation for service of carriage of passengers and freight performed within the Philippines. (Japan Air Lines, Inc. vs. Commissioner of Internal Revenue, CTA Case No. 2480, January 15, 1982.) The important factor which determines the source of income, if from services, for purposes of income taxation, is the place where services are actually rendered. (Mertens, Law of Federal Taxation, Vol. 8, Chap. 45, p. 141.) Income derived from transportation is considered to be income from services, with the result that where the services are rendered determines the source. (Daiichi

Chuo Kisen Kaisha vs. Commissioner of Internal Revenue, CTA Case No. 1277, May 31, 1969.)

However, it is an admitted fact that petitioner did not lift nor land passengers or cargo in the Philippines during the years in question. BOAC was without landing rights for traffic purposes in the Philippines as it was not granted by the then Civil Aeronautics Board (CAB) a certificate of public convenience and necessity to operate in the Philippines. Invariably, any leg or portion of the trips serviced by BOAC commenced outside the Philippines and terminated also outside the Philippines. It is thus clear beyond doubt that since no service of carriage of transportation of passengers or freight was performed by petitioner within the Philippines, the income derived by it from the sales of passage tickets in the Philippines for international air transportation service is not subject to Philippine income tax. Pursuant to Section 24(b)(1) of the Tax Code, as amended, a foreign corporation, whether resident or non-resident, is taxable only on income from "sources within the Philippines".

We see no significance therefore in the special and affirmative defenses of respondent that petitioner is a resident foreign corporation or a non-resident foreign corporation liable to Philippine income tax on income from sources within the Philippines, considering that the travelled revenue derived by BOAC from sales of tickets in the Philippines for international air service is not income derived from sources within the Philippines. Nonetheless, some stress was placed by respondent on the activities of the general sales agent of petitioner of (1) selling and issuing tickets; (2) breaking down the whole trip into a series of trips - each trip in the series corresponding to a different airline company; (3) receiving the fare from the whole trip; (4) subsequently allocating to the various airline companies on the basis of their participation in the service rendered through the mode of "interline settlement" as prescribed by Article VI of Resolution No. 850 of the IATA Agreement; and (5) other activities of advertising, promotions, public relations, acceptance of payments of tickets, and submitting itself to the jurisdiction of our courts in matters relating to these activities in the Philippines as incontrovertible facts that BOAC was engaged in business within the Philippines or had an office or place of business in the Philippines during the period in question. (pp. 238-239, CTA records.)

However, the ruling in Japan Air Lines vs. Commissioner of Internal Revenue, CTA Case No. 1634, November 29, 1968, on which petition for review on certiorari was denied by the Supreme Court in L-30041, February 3, 1969, the factual setting of which is on all fours with the case at bar, to the effect that the acts of a foreign corporation engaged in the business of international air carriage of (a) selling passage tickets in the Philippines through its agent; (b) maintenance of an office in the Philippines for promotion and information purposes; and (c) receipt of payments for passage tickets sold in the Philippines from passengers from the Philippines do not make the taxpayer therein engaged in business in the Philippines, resolves the identical problem now brought before us in these proceedings. The clear intent of the above arrangement, as prescribed in the IATA Agreement, is to save the passenger the trouble of purchasing tickets at the point of departure of every leg of the entire trip. (Japan Air Lines vs. Commissioner of Internal Revenue, supra.) And even on the assumption that petitioner is a resident or non-resident foreign corporation taxable on income from sources within the Philippines, the conclusion that the service of transportation which produced the income sought to be taxed in these appeals took place outside the Philippines foreclosed the non-taxability in the Philippines of the travelled revenue derived by petitioner from the sales of tickets in the country.

After taking the position that petitioner is a foreign corporation, resident or non-resident, liable to income tax on the revenue derived in full from the sales of tickets in the Philippines, respondent in his supporting memorandum would now assume a posture that the travelled revenue derived by BOAC from the sales of tickets in the Philippines for international air transportation service is income derived from sources partly within and partly without the Philippines under Section 37(e) of the Revenue Code.

Again, four-square with the cases at bar on this point, by reason of the exact similarity of the factual settings, the same provision of law involved and the question litigated, is Japan Air Lines, Inc. vs. Commissioner of Internal Revenue, CTA Case No. 2480, January 15, 1982. In holding that the travelled revenue derived by a foreign corporation engaged in the business of international air carriage, as petitioner herein, from sales of tickets in the Philippines for international air transportation service is not income derived from sources partly within and partly without the Philippines, this Court made observations as follows:

> Nevertheless, respondent would attempt to draw support from Section 37(e) of the then in force National Internal Revenue Code which considers income from transportation or other services rendered partly within and partly without the Philippines as income derived from sources partly within and partly without the Philippines. Pursuant to Section 152 of Revenue Regulations No. 2, taxable income from sources within the Philippines includes that derived in full from sources within the Philippines and that portion of the income which is derived partly from sources within and partly from sources without the Philippines which is allocated or apportioned to sources within the Philippines. Since income from the business of transportation service rendered between the Philippines and points outside the Philippines is considered income derived partly from within and partly from without the Philippines under Section 37(e) of the Tax Code, respondent would thus treat revenue derived by petitioner from sales of passage tickets in the Philippines for international air transportation service as income derived from sources partly within and partly without the Philippines.

The argument misses the point. In its textual completeness, the applicable statute provides: "Gains, profits, and income from (1) transportation or other services rendered partly within and partly without the Philippines, x x x x shall be treated as derived partly from sources within and partly from sources without the Philippines." It deals centrally on transportation service rendered partly within and partly without the Philippines. A foreign transportation company derives income partly from sources within and partly from sources without the Philippines if it is carrying on a business of transportation service between points in the Philippines and outside the Philippines. (N.V. Reederiz "Amsterdam" and Royal Interocean Lines vs. Commissioner of Internal Revenue, CTA Case No. 1996, December 1, 1976; Procter & Gamble Philippine Manufacturing Corporation vs. Commissioner of Internal Revenue, CTA Case No. 2437, January 4, 1977; see also Vol. 3, 1965, Federal Taxes, par. 16,381.) Since respondent had admitted - a fact confirmed by this Court in its amended decision in CTA Case No. 1634 - that petitioner did not have planes that lifted or landed passengers and cargo in the Philippines during the period under review as the Japan Air Lines had not yet been granted by the Civil Aeronautics Board a certificate of public convenience and necessity to operate in the Philippines, petitioner could not have carried on a business of transportation service between points in the Philippines and outside the Philippines. Under the circumstances, petitioner during the period under review did not render or could not have rendered, transportation service partly within and partly without the Philippines in order to derive income partly from sources within and partly from sources without the Philippines under Section 37(e) of the Tax Code.

> Moreover, Section 37(e) provides that in the case of gross income derived from sources partly within and partly without the Philippines, the net income should first be computed by deducting the expenses, losses, or other deductions apportioned or allocated thereto and a ratable part of any expenses, losses, or other deductions which cannot definitely be allocated to some items or class of gross income. The portion of such net income attributable to sources within the Philippines may then be determined by processes or formulas of general apportionment prescribed by the Secretary (now Minister) of Finance. As stated earlier, the deficiency income tax assessment under review was based solely on the proceeds of sales of Japan Air Lines passage tickets in the Philippines, which respondent considered income derived in full from sources within the Philippines after deducting sales returns and commissions of the Philippine Air Lines. The fact that the deficiency income tax assessment was based solely on income which respondent considered derived from Philippine sources computed after subtracting deductions to the extent connected with income earned in the Philippines and not on income derived by petitioner from sources partly within and partly without the Philippines determined by the formula of general apportionment prescribed in Section 163 of Revenue Regulations No. 2 in effect negates respondent's allegation that the revenue derived by petitioner from sales of passage tickets in the Philippines is income derived from sources partly within and partly without the Philippines under Section 37(e) of the Tax Code.

The fallacy of respondent's position is his assumption that the source of the income is the place where the transportation tickets is sold, treating such passage tickets for international transportation service as goods sold in the Philippines; and undoubtedly, in order to constitute such income from the sales of tickets derived from sources partly within and partly without the Philippines under Section 37(e) of the National Internal Revenue Code, the tickets would be considered personal property produced (in whole or in part) by petitioner without and sold within the Philippines. As already shown earlier, income from transportation is income from services (not from sale of personal property), with the result that where the services are rendered determines the source. (Daiichi Chuo Kisen Kaisha vs. Commissioner of Internal Revenue, supra.) And as a foreign transportation company, petitioner derived income partly from sources within and partly from sources without the Philippines if it was carrying on a business of transportation service between points in the Philippines and outside the Philippines. (N.V. Reederiz "Amsterdam" and Royal Interocean Lines vs. Commissioner of Internal Revenue, CTA Case No. 1996, December 1, 1976; Procter & Gamble Philippine Manufacturing Corporation vs.

Commissioner of Internal Revenue, CTA Case No. 2437, January 4, 1977; Federal Taxes, Vol. 3, p. 16, 381).

This set-up could be better understood by examining the situation exemplified by Exhibit "L" of petitioner which is admitted by respondent. Thus:

> The BOAC ticket made out by BOAC which is the issuing airline, through Warner Barnes to Mr. Neville covers the latter's trip from Manila to certain foreign destinations and then back to Manila. The travel consists of several legs or sectors, and for every leg the carrying airline as specified in the ticket is different. The first leg is from Manila to London on Qantas; the second from London to Montreal on BOAC; the third from Montreal to Vancouver on Canadian Pacific, then from Vancouver to Hong Kong on Canadian Pacific, and lastly from Hong Kong to Manila on Cathay Pacific. BOAC, the issuing airline has the responsibility of making the reservations and to collect the whole fare for the whole trip. It is, however, Qantas which has, pursuant to the ticket, the responsibility of carrying the passenger and his cargo from Manila to London, and if it is actually Qantas that carries the passenger from Manila to London, that portion of the whole fare corresponding to that leg of the trip, from Manila to London, has to be paid by BOAC to Qantas through the IATA clearing house. Should the passenger, however, for one reason or another not ride on Qantas in the first leg of his trip, but takes instead another airline, the fare corresponding to that leg will be paid, not to Qantas, but to the other airline that actually rendered the service of carrying the passenger from

Manila to London. It appears, therefore, that BOAC, the issuing airline, cannot derive any income from the service of transportation from Manila to London for it is an off-line carrier. In the second leg, from London to Montreal, the passenger may take BOAC according to the ticket. If he does so, that portion of the whole fare corresponding to the leg London to Montreal will be paid to BOAC through the IATA clearing house and BOAC will derive the income from the carriage in that leg. But should the passenger for one reason or another fails or does not like to ride on a BOAC plane in that leg of his trip, but takes another carrier, the corresponding fare will not be paid to BOAC, but will be remitted to the carrier that actually rendered the service. The payment to the carrying carrier that actually rendered the service of transportation will be paid through the IATA clearing house. In the same way, if the passenger takes a Canadian Pacific plane in the third leg of his trip from Montreal to Vancouver, the fare corresponding to said leg will be paid to Canadian Pacific, but if the passenger takes a carrier other than Canadian Pacific, the corresponding fare will be paid not to Canadian Pacific, but to the carrying carrier that rendered actually the service of transportation. The same happens in the fourth leg from Vancouver to Hong Kong, as well as in the fifth leg from Hong Kong to Manila. The passenger may take the carrier as specified in the ticket or he may take another plane, but in every case, the fare corresponding to the leg will be paid through the IATA clearing house to the carrying airline that actually performed the service of transportation. The carrier that actually transports the passenger in every leg of the trip detaches from the ticket issued by BOAC the coupon corresponding to its leg or sector and sends the said coupon to the IATA clearing house where the corresponding disbursements are made to the different airline carriers.

As stated above, the clear intent of this arrangement is to save the passenger the trouble of purchasing tickets at the point of departure of every leg of the entire trip. Under this set-up the conclusion is obvious that BOAC did not engage in the business of a carrier in the Philippines either directly or with the intervention of another carrier that may be considered its extension (Japan Air Lines, Inc. vs. Commissioner of Internal Revenue, supra); much less rendered transportation service between points in the Philippines and outside the Philippines to derive income from sources partly within and partly without the Philippines (N.V. Reederiz "Amsterdam" and Royal Interocean Lines vs. Commissioner of Internal Revenue, supra; Procter & Gamble Philippine Manufacturing Corporation vs. Commissioner of Internal Revenue, supra; Federal Taxes, supra).

Accordingly, the decision of respondent dated February 16, 1972, the petition for reconsideration of which was denied on August 24, 1973:

(a) Denying the request of petitioner for the tax refund or tax credit of the amount of ₱858,307.79 paid by it on January 28, 1970 as income tax, surcharges, interest and compromise penalties for the fiscal years 1959-60 to 1967-68, inclusive, subject of CTA Case No. 2373; and

(b) Reinstating and reissuing the deficiency income tax assessments issued against petitioner for the fiscal years 1968-69 to 1970-71 in the amount of ₱534,132.08, plus 50% surcharge and 1% monthly interest from April 16, 1972 until fully paid, covered in CTA Case No. 2561 cannot be sustained. Respondent Commissioner of Internal Revenue is therefore ordered to credit petitioner British Overseas Airways Corporation the sum of ₱858,307.79, as well as to countermand or cancel the deficiency income tax assessments issued against petitioner in the amount of ₱534,132.08 for the fiscal years 1968-69 to 1970-71.

WHEREFORE, the judgment under review should be as it is hereby reversed.

SO ORDERED.

Quezon City, Metro Manila, January 26, 1983.

AMANTE FILLER
Presiding Judge

WE CONCUR:

CONSTANTE C. ROAQUIN
Associate Judge

ALEX Z. REYES
Associate Judge