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REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

N.V. REEDERIJ "AMSTERDAM"
and ROYAL INTEROCEAN LINES,
Petitioners,

- versus -

C.T.A. CASE NO. 1996

COMMISSIONER OF INTERNAL
REVENUE,
Respondent.

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12/1/76

D E C I S I O N

The question presented by this appeal is whether or not a non-resident foreign shipping corporation, not having any office or place of business in the Philippines, whose vessels called at Philippine ports once a year for two years, derives income partly from sources within and partly from sources without the Philippines and thus taxable on its net income pursuant to Section 24(b)(2) of the Tax Code, in relation to Section 37(e) thereof, or is subject to income tax on its gross income from all sources within the Philippines under Section 24(b)(1) of the same Code.

It appears that petitioners N.V. REEDERIJ "AMSTERDAM" is a shipping corporation organized and existing under the laws of The Netherlands and has its principal office in Hovengebouw, Amsterdam; while petitioner ROYAL INTEROCEAN LINES is likewise a shipping corporation organized and existing under the laws of The Netherlands licensed to do business in the Philippines, with branch office at No. 1010 A. Mabini St., Ermita, Manila. Two vessels owned by N.V. Reederij "Amsterdam", namely, M/V "Amstelmeer" and M/V "Amstelkroon", called at Philippine ports on March 27 to April 10, 1963 and September 24 to October 20, 1964, respectively, for the purpose of loading copra, logs, sugar and other Philippine export products for foreign ports pursuant to affreightment contracts previously negotiated and executed by it and local shippers abroad. Petitioner Royal Interocean Lines acted as husbanding agent for a fee or commission for said vessels. The freight fees on these transactions paid abroad, and which are not disputed, amounted to $98,175.00 in 1963 and $137,193.00 in 1964 as gathered from the accounting records of Royal Interocean Lines.

As there appears no income tax returns filed by petitioners on these freight receipts, respondent, through his examiners, filed the corresponding income tax returns for and in behalf of N.V. Reederij "Amsterdam", pursuant to Section 15 of the National Internal Revenue Code, computing such receipts at the exchange rate of $1.00 to ₱3.90 Philippine pesos. On June 30, 1967 respondent assessed petitioners deficiency income tax for 1963 and 1964 in the amounts of ₱193,973.20 and ₱262,904.94, respectively, computed in accordance with the rate of tax imposed under Section 24(b)(1) of the Tax Code.

On August 28, 1967 Royal Interocean Lines filed returns of the income of the aforementioned vessels derived from the Philippines computed at the exchange rate of U.S. $1.00 to ₱2.00 Philippine pesos and paid the tax due thereon in the amounts of ₱1,835.52 and ₱9,448.94, pursuant to Section 24(b)(2) in relation to Section 37(e) of the National Internal Revenue Code, as implemented by Section 163 of Revenue Regulations No. 2. A written protest on the assessment was filed by petitioners on the same date. In his letter-decision dated March 3, 1969 respondent denied said protest, and after crediting the tax payments made by petitioners in the amounts ₱1,835.52 and ₱9,448.94 for 1963 and 1964, respectively, requested petitioners to pay the balance of ₱192,137.60 and ₱255,088.37 for said years or a total of ₱447,146.05. On March 31, 1969 petitioners instituted the present appeal.

A corporation is itself a taxpaying entity and speaking generally, for purposes of income tax, corporations are classified into (a) domestic corporations and (b) foreign corporations. (Sec. 24(a)(b), Tax Code.) Foreign corporations are further classified into (1) resident foreign corporation and (2) non-resident foreign corporation. (Sec. 24(b)(1) and (2), Tax Code.) A resident foreign corporation is a foreign corporation engaged in trade or business within the Philippines or having an office or place of business therein (Sec. 84(g), Tax Code) while a non-resident foreign corporation is a foreign corporation not engaged in trade or business within the Philippines and not having any office or place of business therein. (Sec. 84(h), Tax Code.)

A domestic corporation is taxed on its income from sources within and without the Philippines, but a foreign corporation is taxed only on its income from sources within the Philippines. (Sec. 24(a), Tax Code; Sec. 16, Rev. Regs. No. 2.) However, 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, Tax Code.) On the other hand, foreign corporations not doing business in the Philippines are 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."

The tax is 30% (now 35%) of such gross income. (Sec. 24(b)(1), Tax Code.)

At the time material to this case, certain corporations were given special treatment, namely, building and loan associations operating as such in accordance with Section 171 of the Corporation Law, educational institutions, domestic life insurance companies and foreign life insurance companies doing business in the Philippines. (Sec. 24(a) & (c), Tax Code.) It bears emphasis, however, that foreign life insurance companies which were not doing business in the Philippines were taxable as other foreign corporations not authorized to do business in the Philippines. (Sec. 24(e), Tax Code).

Now to the case at bar. Here, petitioner N.V. Reederij "Amsterdam" is a non-resident foreign corporation, organized and existing under the laws of The Netherlands with principal office in Amsterdam and not licensed to do business in the Philippines. (pp. 80-81, CTA records.) As a non-resident foreign corporation, it is thus a foreign corporation not engaged in trade or business within the Philippines and not having any office or place of business therein. (Sec. 84(h), Tax Code). As stated above, it is therefore 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, and the tax is equal to thirty per centum of such amount, under Section 24(b)(1) of the Tax Code. The accent is on the words - "of such amount". Accordingly, petitioner N.V. Redeerij "Amsterdam" being a non-resident foreign corporation, its taxable income for purposes of our income tax law consists of its gross income from all sources within the Philippines.

The law seems clear and specific. It thus calls for its application as worded as it leaves no leeway for interpretation. The applicable provision imposes a tax on foreign corporations falling under the classification of non-resident corporations without any exceptions or conditions, unlike in the case of foreign corporations engaged in trade or business within the Philippines which contained (at the time material to this case) an exception with respect to foreign life insurance companies. Adherence to the provision of the law, which specifies and determines the taxable income of, and the rate of income tax applicable to, non-resident foreign corporations, without mentioning any exceptions, would therefore lead to the conclusion that petitioner N.V. Rederij "Amsterdam" is subject to income tax on gross income from all sources within the Philippines.

After alleging and stating as a fact in their pleadings (See Petition for Review, Memorandum of the Petitioners and Reply to Respondent's Memorandum) that N.V. Rederij "Amsterdam" is a non-resident corporation, which is also the basis of the defense of respondent (par. 10, Affirmative Defenses, Answer), petitioners, however, have suddenly reversed themselves and now submit a thesis that by virtue of two calls of the vessels of N.V. Reederij "Amsterdam" at Philippine Ports, once in 1963 and once also in 1964, it "derived income partly from Philippine sources and partly from sources outside the Philippines, thereby in effect engaging business herein." It is "therefore subject to income tax on its net income, computed pursuant to Sections 24(b)(2) and 37(e) of the Tax Code, as implemented by Section 163 of the Income Tax Regulations, and not on gross income under Section 24(b)(1) of the Tax Code." (p.52, CTA records.)

To our minds, such an argument would seem to be in conflict with petitioners' own allegation that N.V. Reederij "Amsterdam" is a non-resident corporation, which means undeniably that it is not engaged in trade or business in the Philippines and not having any office or place of business therein. At any rate, by this reasoning, petitioners concede at least that for a foreign corporation carrying on a business of transportation to derive income partly from sources within and partly from sources without the Philippines and thus subject to income tax on its net income, computed pursuant to Sections 24(b)(2) and 37(e) of the Tax Code, as implemented by Section 163 of Revenue Regulations No. 2, it must be engaged in trade or business in the Philippines.

Back to the statute. Stated by way of paraphrase, Section 37(e) deals with the determination of the net income taxable in the Philippines where income has been derived from sources partly within and partly without the Philippines. The net income may 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; and the portion of such net income attributable to sources within the Philippines may be determined by processes or formulas of general apportionment prescribed by the Secretary of Finance. And apropos of items of gross income from sources partly within and partly without the Philippines, the law considers as one of them the gross receipts of foreign steamship companies whose vessels touch ports of the Philippines. For a foreign shipping corporation whose vessels touch Philippine ports, the formula of general apportionment set out in Section 163, Revenue Regulations No. 2, applies.

It must be stressed, however, that Section 37(e) of the Code, as implemented by Section 163 of the Regulations, provides the rule for the determination of the net income taxable in the Philippines of foreign steamship company doing business in the Philippines. To assure that non-resident foreign steamship companies not engaged in business in the Philippines and not having any office or place of business herein are not covered therein, the regulations explicitly and clearly provide that "the net income of a foreign steamship company doing business in or from this country is ascertained", under the formula contained therein, "for the purpose of the income tax." The reason is easily discernible. As stated above, the taxable income of non-resident foreign corporation consists of its gross income from all sources within the Philippines. Accordingly, a foreign steamship corporation 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 points outside the Philippines. (Vol. 3, 1965, Federal Taxes, Par. 16,389). Only then does Section 37(e) of the Tax Code, as implemented by Section 163 of the Regulations, apply in computing net income subject to tax. There is no basis therefore for an assertion "that Section 37(e) does not distinguish between a foreign corporation engaged in business in the Philippines and a foreign corporation not engaged in business in the Philippines." (p. 84, CTA records.)

In an attempt to draw support from Section 37(e) of the Tax Code and Section 163 of Revenue Regulations No. 2, petitioners however find comfort in the two calls of the vessels of N.V. Reederij "Amsterdam" at Philippine ports, once in 1963 and once in 1964, which according to

them, is "in effect engaging business herein."
As above stated, it seems that petitioners now take a position contradictory to, or inconsistent with, their pleadings, as the fact alleged by them that N.V. Reederij "Amsterdam" is a non-resident foreign corporation not engaged in trade or business in the Philippines is to be taken as final and true for the purpose of this case. Under Section 2, Rule 129 of the Rules of Court, admissions made by the parties in the pleadings, or in the course of the trial or other proceedings can not be contradicted unless previously shown to have been made through palpable mistake. Nonetheless, one call a year for two years only at a Philippine port, pursuant to an affreightment contract negotiated and executed abroad, can not by any stretch of the imagination be considered as carrying on a trade or business of transportation service between points in the Philippines and points outside the Philippines. N.V. Reederij "Amsterdam" does not even have any office or place of business in the Philippines and its co-petitioner Royal Interocean Lines acted only as the husbanding agent for the purpose of clearing its vessels in and out

of Philippine ports.

It is hardly necessary to add:

> The expression "engaged in business" means the same thing as "carrying on business", and the latter expression has the same meaning as "doing business." The three expressions, either separately or connectedly, convey the idea of progression, continuity, or sustained activity. "Engaged in business" means occupied in business, employed in business. "Carrying on business"does not mean the performance of a single disconnected business act. It means conducting, prosecuting, and continuing business by performing progressively all the acts normally incident thereto, and likewise the expression "doing business", when employed as descriptive of an occupation, conveys the idea of business being done, not from time to time, but all the time. (Lewellyn v. Pittsburgh, B. & L.E.R. Co., 222 Fed. 177).
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> A single, isolated activity or transaction is not sufficient to constitute a business. (1955 PH Fed. Taxes, Par. 11008.)
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> Business implies continuity of transaction. (Alexander Howden & Co., LTD. et al., v. Collector (Now Commissioner) of Internal Revenue, G.R. No. L-19392, April 14, 1965, 13 SCRA 601).

Reduced to its simple terms, the one call in 1963 and in 1964 of the vessels of N.V. Reederij "Amsterdam" at Philippine ports, pursuant only to affreightment contracts negotiated and executed abroad, did not constitute carrying on a trade or business of trasportation service between points in the Philippines and points outside the

Philippines to derive income partly from sources within and partly from sources without the Philippines and thus subject N.V. Reederij "Amsterdam" to income tax on its net income computed pursuant to Sections 24(b)(2) and 37(e) of the Tax Code, as implemented by Section 163 of Revenue Regulations No. 2.

In concluding their arguments, petitioners seek final refuge in the amendment by Presidential Decree No. 69 of Section 24(b)(2), which provides that international carriers are subject to tax of 2-1/2% on their gross Philippine billings. The amendatory decree classifying international carries as taxable under Section 24(b)(2) and not under Section 24(b)(1), according to petitioners, is a repudiation of respondent's stand on this case. Considering that this case involves the years 1963 and 1964, that is, prior to the effectivity of said decree, the amendment to the law has no controlling effect to the instant appeal. Tax laws are prospective in operation and there is nothing in Section 24(b)(2), as amended by Presidential Decree No. 69, that provides for its retroactive effect or from which we can imply the intent that it operates retrospectively. (Lorenzo v. Posadas, 64 Phil. 353; Comm. v. Filipinas Cia de Seguros, 107 Phil. 1055.) It will be noted, however, by way of observation only, that Section 24(b)(2) imposes a tax on a corporation organized, authorized, or existing under the laws of any foreign country, engaged in trade or business within the Philippines, and petitioner N.V. Reederij "Amsterdam" is admittedly a non-resident foreign corporation not engaged in trade or business within the Philippines and not having any office or place of business herein.

In their petition for review, petitioners also raise the question as to the propriety of the use by respondent of the exchange rate of US $1.00 to ₱3.90 in determining their gross income from Philippine sources in pesos and computing their income tax on the equivalent thereof. It appears that no decision was rendered by respondent on this issue as it was not raised in the Bureau of Internal Revenue. Without in the least attempting to express an opinion as to whether or not this

Court, in the exercise of its appellate power to review decisions of the Commissioner of Internal Revenue involving disputed assessments under Section 7(1) of Republic Act No. 1125, can lawfully take cognizance of this question which is being raised for the first time on appeal, we note that this issue has already been definitely settled by the Supreme Court when it ruled in the case of Commissioner of Internal Revenue v. Royal Interocean Lines and the Court of Tax Appeals, G.R. No. L-26806, July 30, 1970, 34 SCRA 9, that:

> "It should be noted that on July 16, 1959, the policy incorporated in Circular No. 20 and implemented in subsequent circulars was relaxed with the enactment of Republic Act No. 2609 which directed the monetary authorities to take steps for the adoption of a four year program of gradual decontrol, during which the Monetary Board, with the approval of the President, could and did fix the conversion rate of the Philippine peso to the US dollar at a ratio other than that prescribed in Section 48 of Republic Act 265. During the period involved in the case at bar, the free market conversion rate ranged from ₱3.47 to ₱3.65 to a US dollar at which rate the freight fees in question were computed in the contested assessment. Inasmuch as said fees were revenues derived from "foreign exchange" transactions, it follows necessarily that the petitioner was fully justified in computing the taxpayer's receipts at said free market rates."
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> "The case of the United States Lines, on which the appealed decision of the Court of Tax Appeals is anchored, refers to transactions that took place before the approval of Republic Act 2609 on July 16, 1959 when the only legal rate of exchange obtaining in the Philippines was ₱2 to $1, and all foreign exchange had to be surrendered

> to the Central Bank subject to its disposition pursuant to its own rules and regulations. Upon the other hand, the present case refers to transactions that took place during the effectivity of Republic Act 2609 when there was, apart from the parity rate, a legal free market conversion rate for foreign exchange transactions, which rate had been fixed in open trading, such as those involved in the case at bar."

This case involves taxable years 1963 and 1964, during the effectivity of Republic Act No. 2609, and it appears that the free market conversion rate at that time was ₱3.90 to U.S. $1.00. It follows that no error was committed by respondent in this regard.

Respondent imposed the 50% surcharge authorized under Section 72 of the Tax Code because the income tax returns of petitioners for the years 1963 and 1964 were filed only on August 28, 1967, after respondent's examiners had already finished their examination and after petitioners had received the assessment in this case based on the income tax returns prepared and filed by respondent for and in behalf of petitioners pursuant to Section 15 of the Tax Code. In case of willful neglect to file the return within the time prescribed by law, the Commissioner of Internal Revenue under Section 72 of the Tax Code, should add to the tax or to the deficiency tax a surcharge of 50% of the amount of such tax or deficiency tax.

Respondent based his conclusion that there was willful neglect on the part of petitioners to render the returns within the time prescribed by law because under the then existing internal revenue laws, every corporation subject to tax should render a true and accurate return of its annual income on or before the fifteenth day of April of each year for the preceding calendar year, or if the corporation had designated a fiscal year, on or before the fifteenth day of the fourth month following the close of each fiscal year. (Sec. 46(a)(b), Tax Code.) Considering that petitioner N.V. Reederij "Amsterdam" is on the calendar year basis, its annual return for 1963 should have been filed on or before April 15, 1964, and with respect to the calendar year 1964, on or before April 15, 1965.

As no returns were filed by petitioners, respondent, after investigation conducted by his examiners, filed the corresponding income tax returns for and in behalf of them pursuant to Section 15 of the Revenue Code. Respondent in his letter dated March 2, 1967 then invited the president/general manager of petitioner

Royal Interocean Lines for a conference on the findings of his investigating examiners but he failed to receive a reply. Respondent forthwith issued a letter of demand dated June 30, 1967, together with the assessment in question. Subsequently, on August 28, 1967 petitioner Royal Interocean Lines filed returns on the income of N.V. Reederij "Amsterdam" in the Philippines computed at the exchange rate of ₱2.00 to U.S. $1.00 and paid the tax due thereon in the amounts of ₱1,835.52 and ₱9,448.94, on the assumption that the latter is a foreign corporation engaged in trade or business in the Philippines.

While it is true that when Royal Interocean Lines filed the returns on the income of N.V. Reederij "Amsterdam", respondent had already investigated petitioners and the latter had already received respondent's assessment, it can hardly be said that there was deliberate and willful neglect to render returns by petitioners considering that the returns were filed voluntarily and the tax due thereon paid without notice from respondent. It should be noted that petitioner Royal Interocean Lines acted as the vessel's husbanding agent in the Philippines only for the purpose of clearing it in and out of Philippine ports and attending to its needs; Royal Interocean Lines had no authority to collect, and did not collect, the freight, and its compensation consisted of a flat rate fee of $250.00 per vessel per voyage, without any relation to the freight. It had no knowledge of the income and expenses incurred by N.V. Reederij "Amsterdam" from the voyages of its vessels to and from Philippine ports. And N.V. Reederij "Amsterdam", being a non-resident foreign corporation not engaged in trade or business in the Philippines, is not conversant with our tax laws. To impose the 50% surcharge for failure to render returns when the intention of petitioners to deliberately and willfully evade payment of the tax due them had not been clearly established would, therefore, be not only unfair but also tantamount to imposing a penalty based upon a mere vague inference that there was intent to defraud the Government of its lawful revenue, which was not duly proven.

It is to be emphasized, however, that petitioners failed to file the income tax returns within the time prescribed by law. Since their failure to render the returns was not due to an honest belief that they were not taxable or that they were under no obligation to file a return, the 25% surcharge also authorized under Section 72 of the Tax Code should be imposed. With this modification, the appealed decision must therefore stand. In fine, petitioners are liable for deficiency income tax for the years 1963 and 1964 in the respective amount of ₱162,421.43 and ₱213,879.37, or a total of ₱376,300.80, computed as follows:

1963

Net Income per investigation	₱382,882.50
Income tax due thereon	114,865.00
Add: 25% surcharge	28,716.25
1/2% mo. int. from 4-16-64 to 4-16-67	20,675.70
Total	₱ 164,256.95
Less: payment on 8-28-67	1,835.52
Balance	₱ 162,421.43

1964

Net Income per investigation	₱ 532,052.00
Income tax due thereon	160,516.00
Add: 25% surcharge	40,129.00
1/2% mo. int. from 4-20-65 to 6-28-67	22,683.31
T o t a l	₱ 223,328.31
Less: payment on 8-28-67	9,448.94
Balance	₱ 213,879.37
Total amount still Due and Collectible	₱376,300.80

The compromise penalty in the total amount of ₱2,000.00 (₱1,000 each for 1963 and 1964) suggested by respondent in his assessment should not be imposed or collected without the agreement and conformity of petitioners. And it does not appear that petitioners accepted the imposition of the compromise amount. (Wonder Mechanical Engineering Corporation v. Court of Tax Appeals, G.R. Nos. L-22805 and L-27858, June 30, 1975, 64 SCRA 555; See also; Collector of Internal Revenue v. University of Santo Tomas, G.R. Nos. L-11274 & L-11280, Nov. 28. 1958, 104 Phil. 1062, Unpub.; Phil. International Fair, Inc. v. Collector of Internal Revenue, G.R. Nos. L-12928 & L-12932, March 31, 1962, 4 SCRA 774.) Accordingly, petitioners N.V. Reederij "Amsterdam" and Royal Interocean Lines are ordered, jointly and severally, to pay to respondent Commissioner of Internal Revenue the amounts of ₱162,421.43 and ₱213,879.37 as deficiency income tax for the years 1963 and 1964, respectively, or a total of ₱376,300.80 plus the surcharge and interest which have accrued thereon incident to delinquency, pursuant to Section 51(e) of the National Internal Revenue Code, as amended.

WHEREFORE, the appealed decision is hereby modified in the sense that the 50% surcharge added to the deficiency tax is reduced to 25%, and is affirmed in all other respects. With costs against petitioners.

SO ORDERED.

Quezon City, December 1, 1976.

AMANTE FILLER
Associate Judge

WE CONCUR:

ESTANISLAO R. ALVAREZ
Presiding Judge

CONSTANTE C. ROAQUIN
Associate Judge