REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

FIRST DIVISION

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SOUTH AFRICAN AIRWAYS,
Petitioner,

C.T.A. CASE NO. 6760

- versus -

Members:

ACOSTA, *Chairman*
BAUTISTA, and
CASANOVA, *JJ.*

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:
JUN 09 2005
GMApolinario

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DECISION

BAUTISTA, L., J.:

Submitted for decision is petitioner's claim for refund in the amount of TWO MILLION SIX HUNDRED NINETY THOUSAND FORTY NINE PESOS & EIGHTY ONE CENTAVOS (₱2,690,049.81) alleged to have been erroneously paid as tax on Gross Philippine Billings for the taxable year 2001.

The undisputed facts are as follows:[1]

Petitioner is a nonresident foreign corporation organized and existing under the laws of the Republic of South Africa with principal office at Airways Park, Jones Road, Johannesburg International Airport, South Africa 1672. It is an off-line international air carrier having no landing rights in the Philippines and it does not

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[1] Culled from the parties' Joint Stipulation of Facts and Issues and from the evidence on record.

maintain flight operations to and from the Philippines. Instead, petitioner maintains off-line flights for the carriage of passengers and cargo between ports or points outside the territorial jurisdiction of the Philippines.

By its own admission and as established by evidence, petitioner is not registered with the Securities and Exchange Commission as a corporation, branch office or partnership. Simply put, is not licensed to do business in the Philippines.

Petitioner, however, has Aerotel Limited Corporation as its general sales agent in the Philippines that, among other things, sells passage documents for compensation or commission covering its off-line flights.

For taxable year 2001, petitioner's sales agent filed on its behalf four (4) separate Quarterly Income Tax Returns for passenger and cargo with the Bureau of Internal Revenue on the following dates:

PERIOD	PASSENGER		CARGO	
	Date Filed	Exhibit	Date Filed	Exhibit
1st Quarter	5/30/2001	G	5/30/2001	C
2nd Quarter	8/29/2001	H	8/29/2001	D
3rd Quarter	11/29/2001	I	11/29/2001	E
Final Adjustment Return	4/15/2002	J	4/15/2002	F

On the belief that it is entitled to a refund, petitioner filed a formal claim for refund with respondent, through Revenue District Office No. 47 of the Bureau of Internal Revenue on February 5, 2003 for the recovery of the amount of P2,690,049.81 representing erroneously paid tax on Gross Philippine Billings for taxable year 2001.

Up to this date, however, respondent has not acted on the petitioner's claim for refund and petitioner is now seeking relief from the Court.

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Both parties submit the following issues for the Court's determination:

1. Whether petitioner complied with the requirements under Section 204 and 229 of the National Internal Revenue Code of 1997 for the recovery of internal revenue taxes that have been erroneously, wrongfully, illegally or excessively assessed or collected;

2. Whether gross revenues derived by an off-line carrier from the carriage of passengers and cargo between ports or points outside the territorial jurisdiction of the Philippines, through the sale of passage documents in the Philippines by the off-line carrier's sales agent, are subject to the Gross Philippine Billings tax; and

3. Whether or not petitioner is entitled to the refund of erroneously paid tax on Gross Philippine Billings for taxable year 2001 in the amount of P2,690,049.81.

The Court finds no merit to grant petitioner's prayer for reliefs.

The Court shall dispense with the determination of the first issue as both parties already stipulated on the fact that petitioner filed both the administrative and the judicial claims for refund for the alleged erroneously paid tax for the year 2001 within the prescriptive period.

As regards to the second and third issues, petitioner submits that it is not liable to pay the Gross Philippine Billings tax as it is a foreign airline company with off-line flights. Based on its petition and memorandum, petitioner's arguments are summed up as follows:

1. Under Section 28(A)(3)(a) of the NIRC and Revenue Regulations No. 15-2002, the said tax shall apply only to gross revenues derived from the carriage of persons, excess baggage, cargo and mail that originate from the Philippines in a continuous and uninterrupted flight. The determining factor of tax on international air carrier is the place where the carriage of passengers and cargo originated and not the place of sale of tickets;

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2. The fact that it has a general sales agent in the Philippines does not amount to "doing in business in the Philippines" and, therefore, it is not liable to pay the tax on gross Philippine billings. As a matter of fact, in VAT Ruling No. 03-04 (dated February 13, 2004), respondent categorically recognized that petitioner is not engaged in business in the Philippines;

3. It renders services outside the Philippines and its income derived therefrom are income from sources without the Philippines. Thus, it is not subject to Philippine income tax.

Respondent opposes the petitioner's claim for refund basically on two grounds: (1) the transaction periods mentioned in the petition are not covered by RR No. 15-2002 as the same became effective only on October 26, 2002; and, (2) granting that petitioner is not liable to pay the said tax, it is still liable to pay tax equal to 32% of its gross income received during the taxable year 2001 from all sources within the Philippines for being a non-resident foreign corporation pursuant to Section 28 (B)(1) of the NIRC.

Section 28 (A)(3)(a) of the National Internal Revenue Code of 1997 ("NIRC") provides for the tax on Gross Philippine Billings of international air carriers. It states that:

SECTION 28. *Rates of Income Tax on Foreign Corporations.* —

(A) *Tax on Resident Foreign Corporations.* —

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(3) *International Carrier.* — An international carrier doing business in the Philippines shall pay a tax of two and one-half percent (2 ½%) on its 'Gross Philippine Billings' as defined hereunder:

> (a) *International Air Carrier.* — *'Gross Philippine Billings'* refers to the amount of gross revenue derived from carriage of persons, excess baggage, cargo and mail originating from the Philippines in a continuous and uninterrupted flight, irrespective of the place of sale or issue and the place of payment of the ticket or passage document: *Provided*, That tickets revalidated, exchanged and/or indorsed to another international airline form part of the Gross Philippine Billings if the passenger boards a plane in a port or point in the Philippines: *Provided, further*, That for a flight which originates from the Philippines, but transshipment of passenger takes place at any port outside the Philippines on another airline, only the aliquot portion of the cost of the ticket corresponding to the leg flown from the Philippines to the point of transshipment shall form part of Gross Philippine Billings.

The Court held recently in *Air Canada vs. Commissioner of Internal Revenue*:[2]

"xxx [I]t is evident that the definition of 'Gross Philippine Billings' under Section 28(A)(3)(a) of the 1997 Tax Code covers the gross revenue derived from the carriage of persons, excess baggage, cargo and mail '*originating from the Philippines in a continuous and uninterrupted flight*' irrespective of the place or sale or issue and the place of payment of the ticket or passage document. 'To originate' would mean 'to cause the beginning of; to start (a person or thing) on a course or journey; to begin, start' (Webster's Third New International Dictionary). In other words, the flights carrying the passengers must have originated or started from the Philippines. Verily, petitioner, being an off-line international carrier, as authorized to operate by the Civil Aeronautics Board (*Exhibit 'I'*) and having no flights originating from the Philippines in a continuous and uninterrupted flight, cannot be taxed pursuant to Section 28(A)(3)(a) of the 1997 Tax Code, that is, based on their Gross Philippine Billings."

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2 CTA Case No. 6572, December 22, 2004.

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The Court, however, ruled that petitioner *Air Canada* was still liable to pay income tax. We quote:

> "Under Section 22 of the 1997 Tax Code, the term 'resident foreign corporation' applies to a foreign corporation engaged in trade or business within the Philippines, while the term 'non-resident foreign corporation' applies to a foreign corporation not engaged in trade or business within the Philippines. However, with regard to the term 'doing' or 'engaged in' business, there is no fixed or specific criterion as what constitutes 'doing' or 'engaging' in business. In the case of *The Mentholatum Co., Inc., et al. vs. Mangiliman, et al., 72 PHIL 524*, the Honorable Supreme Court had thoroughly and clearly explained the term in this way:
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> > "'...There is *no specific criterion as to what constitutes 'doing' or 'engaging in'* or *'transacting'* business. Each case must be judged in the light of its peculiar environmental circumstances. The term implies *continuity of commercial dealings and arrangements*, and contemplates, to that extent, the performance of acts or works or the exercise of some of the functions normally incident to, and in progressive prosecution of commercial gain or for the purpose and object of the business organization.' xxx
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> "In order that a foreign corporation may be regarded as doing business, there must be continuity of conduct and intention to establish a continuous business, such as the appointment of a local agent, and not one of a temporary character. In other words, a foreign airline company selling tickets in the Philippines through their local agents, whether liaison offices, agencies or branches, as in the case at bar, shall be considered as resident foreign corporation engaged in trade or business in that country for such activities show continuity of commercial dealings or arrangements and performance of acts or works or the exercise of some functions normally incident to and in progressive prosecution of commercial gain or for the purpose and object of the business organization."

In the present case, the Court maintains that while petitioner is not liable to pay tax on Gross Philippine Billings, it is still liable to pay income tax on its gross revenue from the sales of its passage documents. Section 27(A) of the NIRC provides:

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> SECTION 27. *Rates of Income Tax on Domestic Corporations.* —
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> (A) *In General.* — Except as otherwise provided in this Code, **an income tax of** thirty-five percent (35%) **is hereby imposed upon the taxable income derived during each taxable year from all sources within and without the Philippines by every corporation, as defined in Section 22(B) of this Code** and taxable under this Title as a corporation, organized in, or existing under the laws of the Philippines: *Provided*, That effective January 1, 1998, the rate of income tax shall be thirty-four percent (34%); effective January 1, 1999, the rate shall be thirty-three percent (33%); **and effective January 1, 2000 and thereafter, the rate shall be thirty-two percent (32%).**

In relation thereto, Section 32 of the same Code further gives Us the meaning of gross income as "all income derived from whatever source, including but not limited to compensation for services in whatever form paid, including, but not limited to fees, salaries, wages, commissions, and similar items, gross income derived from the conduct of trade or business or the exercise of a profession; gains derived from dealings in property; interests; rents; royalties, dividends; annuities; prizes and winnings; pensions; and partner's distributive share from the net income of the general professional partnerships."

The above definition is so broad and encompassing that discloses the legislative intent to include all income not expressly exempted. Applying the said definition to the present case, proceeds from sales of passage documents by the petitioner are subject to income tax. This conclusion is not without logic. It has been consistently ruled that the source of income is the property, activity or service that produced the income and, in order that the source of income to be considered

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as coming from the Philippines, it is enough that the income is derived from activity within the Philippines.[3]

The absence of flight operations to and from the Philippines is not determinative of the source of income or the situs of income taxation. Petitioner admitted that it sells passage documents in the Philippines through its sales agent. Petitioner, thus, is deriving revenues from the conduct of its business activity regularly pursued within the Philippines. Petitioner is therefore a resident foreign corporation engaged in trade or business in the country within the purview of our tax law and is therefore subject to tax. As held in *Commissioner of Internal Revenue vs. American Airlines, Inc.*:[4] "xxx foreign airline companies which sold tickets in the Philippines through their local agents, whether called liaison offices, agencies or branches, were considered resident foreign corporations engaged in trade or business in the country. Such activities show continuity of commercial dealings or arrangements and performance of acts or works or the exercise of some functions normally incident to and in progressive prosecution of commercial gain or for the purpose and object of the business organization."

In *Commissioner of Internal Revenue vs. British Overseas Airways, Corp.*,[5] the Supreme Court has categorically ruled that:

> "The absence of flight operations to and from the Philippines is not determinative of the source of income or the situs of income taxation. xxx The test of taxability is the 'source'; and the source of an income is that activity xxx which produced the income. Unquestionably, the passage documentations in these cases were sold in the Philippines

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3 *Manila Gas Corp. vs. Collector of Internal Revenue*, 62 Phil. 895 [1935]; *Commissioner of Internal Revenue vs. Japan Air Lines, Inc.*, 202 SCRA 450 [1991]; and, *Commissioner of Internal Revenue vs. Air India*, 157 SCRA 648 [1988].

4 180 SCRA 274 [1989].

5 149 SCRA 395 [1987].

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> and the revenue therefrom was derived from a business activity regularly pursued within the Philippines. And even if the BOAC tickets sold covered the 'transport of passengers and cargo to and from foreign cities', it cannot alter the fact that income from the sale of tickets was derived from the Philippines. The word 'source' conveys one essential idea, that of origin, and the origin of the income herein is the Philippines."

Petitioner, as resident foreign corporation engaged in trade or business in the Philippines, is not liable to pay tax on Gross Philippine Billings as provided in Section 28(A)(3)(a) of the Tax Code. However, it is still liable to pay thirty two percent (32%) of its taxable income derived from its sales of passage documents here in the Philippines. Hence, the petition should be dismissed.

WHEREFORE, premises considered, the Petition for Review is hereby **DISMISSED** for utter lack of merit.

SO ORDERED.

LOVELL R. BAUTISTA
Associate Justice

WE CONCUR:

(On Leave)
ERNESTO D. ACOSTA
Presiding Justice

CAESAR A. CASANOVA
Associate Justice

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CERTIFICATION

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

LOVELL R. BAUTISTA
Senior Associate Justice

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