REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

EN BANC

COMMISSIONER OF INTERNAL REVENUE, Petitioner,	**C.T.A. EB No. 242**
	(C.T.A. Case No. 6734)
	Present:
- versus -	**Acosta , *P.J.,*** **Castañeda, Jr.,** **Bautista,** **Uy,** **Casanova,** **Palanca-Enriquez, *JJ.***
PHILIPPINE AIRLINES, INC. (PAL), Respondent.	**Promulgated:** SEP 1 1 2007 GAApolinario

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DECISION

ACOSTA, *P.J.*:

This is a Petition for Review *En Banc* seeking the reversal and setting aside of the Decision of this Court's Second Division dated October 13, 2006, and the subsequent Resolution dated December 8, 2006, affirming the assailed Decision, which ordered herein petitioner Commissioner of Internal Revenue (CIR) to refund or to allow a tax credit to herein respondent Philippine Airlines, Inc. (PAL) the amount of P1,048,375.13, representing the 20% and 7½% final income tax withheld by depository banks on interest income and remitted to herein petitioner for the calendar year 2001.

The antecedent facts as culled from the records are as follows:

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Petitioner is the Commissioner of the Bureau of Internal Revenue (BIR), which is the government agency in charge of the assessment and collection of all national internal revenue taxes, fees, and charges, including the 20% final income tax on interest on currency bank deposits and yield or any other monetary benefit from deposits substitutes and from trust fund and similar arrangements received by domestic corporations, and the 7½% final income tax on interest income derived by a domestic corporation from a depository bank under the expanded foreign currency deposit system, imposed under Sec. 27(D)(1) of the National Internal Revenue Code (NIRC). Its principal office is at the BIR National Office Building, Agham Road, Diliman, Quezon City.

Respondent PAL is a domestic corporation organized in accordance with the laws of the Republic of the Philippines, with principal office at the 9th Floor, PAL Center, Legaspi St., Legazpi Village, Makati City.

On November 28, 2002, respondent filed with petitioner a written request for the refund of the amount of P540,000.00 and US$9,886.06 pertaining to the total amount of final withholding taxes withheld from respondent by International Exchange Bank (IEB) and Philippine Bank of Communication (PBC) for the year 2001. As elaborated in the letter, respondent's request for refund is anchored on its exemption from final withholding tax under its franchise, Presidential Decree (P.D.) No. 1590.

Petitioner's inaction on its request prompted respondent to file a Petition for Review before the Court of Tax Appeals (CTA) on July 24, 2003.

During trial, respondent submitted testimonial and documentary evidence, while petitioner manifested for the submission of the case for decision without presenting any evidence.

On October 13, 2006, the CTA Second Division (Second Division) promulgated the assailed Decision granting the Petition for Review.

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On November 3, 2006, petitioner filed a Motion for Reconsideration, but it was denied in a Resolution dated December 8, 2006.

After the Court granted a 15-day extension, petitioner filed the instant Petition for Review *En Banc* on January 12, 2007 raising the lone issue of "**whether or not respondent is entitled to the claim for refund of the final withholding tax on its bank deposits**."

In arguing its claim, petitioner quoted a portion of the Second Division's Decision, to wit:

> "The 'in lieu of all other taxes' clause under Section 13 of petitioner's legislative franchise, ***exempts PAL from all taxes necessary in the conduct of its business covered by the franchise***, except tax on its real property for which PAL is expressly made liable."

Relying on the above-quoted portion, petitioner now claims that the phrase "in lieu of all taxes" in Section 13 of PD 1590 applies only to taxes necessary in the conduct of its business covered by the franchise. Thus, the prevailing intent of the Section is to exempt respondent only from the payment of such taxes.

Petitioner continues that since the final taxes withheld on the interest income of respondent's investments in dollar/peso placements and time deposit accounts are taxes on income on investments and not income coming from the conduct of business, then such tax is proper and cannot be the subject of a refund or issuance of tax credit.

We disagree.

The issue at hand revolves on the correct interpretation of **Section 13 of P.D. 1590**[1], which is quoted as follows:

> "Sec. 13. In consideration of the franchise and rights hereby granted, the grantee shall pay to the Philippine Government during the life of this franchise whichever of subsections (a) and (b) hereunder will result in a lower tax:

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[1] An Act Granting a New Franchise to Philippine Airlines, Inc. To Establish, Operate, And Maintain Air-Transport Services In the Philippines And Between the Philippines and Other Countries.

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a. The basic corporate income tax based on the grantee's annual net taxable income computed in accordance with the provisions of the National Internal Revenue Code; or

b. A franchise tax of two per cent (2%) of the gross revenues derived by the grantee from all sources, without distinction as to transport or non-transport operations; provided, that with respect to international air-transport service, only the gross passenger, mail, and freight revenues from its outgoing flights shall be subject to this tax.

The tax paid by the grantee under either of the above alternatives shall be in lieu of all other taxes, duties, royalties, registration, license, and other fees and charges of any kind, nature, or description, imposed, levied, established, assessed, or collected by any municipal, city, provincial, or national authority or government agency, **now or in the future**, including but not limited to the following:

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The grantee, shall, however, pay the tax on its real property in conformity with existing law." (*Emphasis supplied*)

Apparently from the foregoing, respondent has the option to pay either the basic corporate income tax or the franchise tax of 2% whichever is lower. The option chosen would be "in lieu of" all other taxes.

The phrase "in lieu of" means "instead of; in place of; in substitution of. It does not mean "in addition."[2] In other words, whichever is lower between the options granted to respondent would be its "tax payable" in place of or in substitution of all other taxes including the 20% and 7½% final withholding taxes which are the subject taxes of herein petition. Upon payment, respondent PAL is already exempted from paying all other taxes, except real property tax for which it is expressly made liable.

Section 13 of P.D. 1590 is devoid of any distinction or further requirement that the taxes from which PAL is exempted must pertain only to those which are necessary in the conduct of its business.

[2] Black's Law Dictionary 6th Edition page 787

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It bears stressing that Courts may not, in the guise of interpretation, enlarge the scope of a statute and include therein situations not provided nor intended by the lawmakers.[3] Statutes that are clear, plain and specific should be applied without further construction and interpretation. Thus, "where a provision of law expressly limits its application to certain transactions, it cannot be extended to other transactions by interpretation."[4]

To remove all doubts, the Supreme Court itself had already clarified the meaning of Section 13 of P.D. 1590 in the case of **The Commissioner of Internal Revenue vs. Philippine Airlines, Inc.**;[5] the pertinent portion of which is hereby quoted:

> "A franchise is a legislative grant to operate a public utility. Like those of any other statute, the ambiguous provisions of a franchise should be construed in accordance with the intent of the legislature. In the present case, Presidential Decree 1590 granted Philippine Airlines an option to pay the lower of two alternatives: (a) 'the basic corporate income tax based on PAL's annual net taxable income computed in accordance with the provisions of the National Internal Revenue Code' or (b) 'a franchise tax of two percent of gross revenues.' Availment of either of these two alternatives shall exempt the airline from the payment of 'all other taxes,' including the 20 percent final withholding tax on bank deposits
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> A corporate income tax liability, therefore, has two components: the general rate of 35 percent, which is not disputed; and the specific final rates for certain passive incomes. PAL's request for a refund in the present case pertains to the passive income on bank deposits, which is subject to the specific final tax of 20 percent.
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> To repeat, the pertinent provision in the case at bar reads: 'basic corporate income tax based on the grantee's annual net taxable income computed in accordance with the provisions of the National Internal Revenue Code.' The Court has already illustrated that, under the Tax Code, 'taxable income' does not include passive income subjected to final withholding taxes. Clearly, then, the 'basic corporate income tax' identified in Section 13 (a) of the franchise relates to the general rate of 35 percent as stipulated in Section 27 of the Tax Code. The final 20 percent taxes disputed in the present case

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[3] Lapid v. CA, G.R. No. 142261, June 29, 2000, 334 SCRA 738, 753; quoting Morales v. Subido, G.R. No. 29658, November 29, 1968, 26 SCRA 150

[4] Canet v. Decena, G.R. No. 155344, January 20, 2004, 420 SCRA 388

[5] G.R. No. 160528, October 9, 2006

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are not covered under Section 13 (a) of PAL's franchise; thus, a refund is in order.

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xxx. It is clear that PD 1590 intended to give respondent the option to avail itself of Subsection (a) or (b) as consideration for its franchise. Either option excludes the payment of other taxes and dues imposed or collected by the national or the local government. PAL has the option to choose the alternative that result in lower taxes. It is not the fact of tax payment that exempts it, but the exercise of its option."

Petitioner's reliance on the phrase "all taxes necessary in the conduct of its business covered by the franchise" appearing in the assailed Decision is misplaced. Such strained and restrictive interpretation of the Decision is clearly unwarranted. When the Decision is carefully and thoroughly read, it reveals that it was never intended to limit the exemption of PAL only from taxes which are necessary in the conduct of its business.

Noteworthy is the fact that the Decision neither dwelt nor persisted on the phrase as a basis for concluding the issue at hand. On the contrary, when the Decision is read as whole, it shows that the real intendment thereof is to refer to "all taxes" regardless of whether they are necessary or not in the conduct of its business.

To exemplify the true meaning of the Decision, the following portions, among others, are hereby quoted:

"***Rationale of the Exemption***

The rationale or purpose for the exemption from **all other taxes** except the income tax and real property tax granted to petitioner PAL upon the payment of the basic corporate income tax or the 2% franchise tax is that such exemption is part of the inducement for the acceptance of the franchise and the rendition of public service by the grantee. To repeat, the only qualification provided for in the law is the option given to PAL to choose between the taxes which will yield the lesser liability.

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To conclude, **the final tax on interest income of bank deposit is regarded to belong to 'other taxes' as it was not included in the choices provided by the franchise.** To hold otherwise would be to give

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> another option to petitioner which is evidently not within the ambit of P.D. 1590.[6]" *(Emphasis supplied)*

The fact still remains that P.D. 1590 exempts respondent PAL from all other taxes except real property tax, and it has the option to pay the lower tax between the basic corporate tax and the 2% franchise tax.

The Second Division explained the rationale of the exemption in the following manner:

> "xxx if We were to impose the final tax on interest income of bank deposits against petitioner, this would effectively negate the rationale of the law, by stripping PAL of the right given to it by virtue of its franchise to avail of tax incentives, such as the 'in lieu of all other taxes' clause.
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> In the event that petitioner results to a no tax liability upon availing of one of the alternatives given, it should not be held liable for any other tax, except for real property tax. This is the clear intendment of *P.D. 1590* which grants a new franchise to herein petitioner PAL.
>
> To conclude, the final tax on interest income of bank deposit is regarded to belong to 'other taxes' as it was not included in the choices provided by the franchise. To hold otherwise would be to give another option to petitioner which is evidently not within the ambit of *P.D. 1590."*

In the case at bar, the Second Division found that respondent PAL opted to pay the basic corporate tax as proved by its Annual Income Tax Returns for the fiscal years ending March 31, 2001 and March 31, 2002. Respondent had a negative income tax liability arising from zero net income. A negative income tax liability is obviously lower than the 2% franchise tax. Consequently, respondent did not pay any income tax. Having exercised the option granted by P.D. 1590, respondent is no longer liable to pay any other taxes. Thus, when final taxes were withheld from its bank deposits and subsequently remitted to petitioner, such constitutes "illegally or erroneously paid taxes" which is a proper subject of refund under Section 204(C) in relation to Section 229 of the NIRC of 1997. For emphasis,

[6] Page 14 of the Decision, *Rollo*, page 35

an erroneous or illegal tax is defined as one levied without statutory authority or upon property not subject to taxation[7].

The Second Division found that respondent PAL was able to prove its entitlement to the refund. However, certain discrepancies were noted resulting in the refundable amount of P1,048,375.132. This was explained in the assailed Decision in this wise:

> "However, We note that there are discrepancies with regard to the conversion rate used by petitioner in its computation of the claimed amount. Petitioner PAL applied the rate of P53.75 to US$1.00 on all its dollar remittances of interest income from bank deposits that resulted in the amount of P1,701,375.72 which should have not been the case. The applied rate of P53.75 has no basis in the evidences presented before the Court. The exchange rate that should have been used in computing the total peso equivalent of the remitted amount is the BSP Exchange Rate indicated on the Remittance Returns (lines 25C and 26C of BIR Form No. 1602) by the respective banks that remitted the withheld taxes in question.
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> Hence, the accurate computation applying the proper exchange rates to all the dollar remittances should have been the following:

BANK	PERIOD COVERED	EXHIBIT	AMOUNT WITHHELD	BSP EXHANGE RATE (P = $1.00)	PESO EQUIVALENT
IEB	June 4, 2001 Sept. 4, 2001 October 4, 2001	"Q" "R" "S"	$3,450.70 $2,827.60 $414.16	P50.58 P52.25 P51.38	174,536.406 147,742.10 21,279.54
PBC	July 2001 August 2001 September 2001	"I" (3rd Quarter)	$350.00 $854.35 $989.25	P51.767	18,118.45 44,227.136 51,210.50
	December 2001 July 2001	"K"	$1,000.00 P540,000.00	P51.261	51,261.00 540,000.00

> Based on the above conversion table, the total amount converted to Philippine peso from the dollar remittances should have been P508,375.132 and not P531,375.72. Therefore, the total amount refundable by petitioner PAL is only P1,048,375.132."

All the foregoing considered, this Court *En Banc* finds no reversible error committed by the Second Division of this Court in rendering the assailed Decision.

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[7] Black's Law Dictionary, 6th Edition page 542

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WHEREFORE, the instant petition is hereby **DENIED** for lack of merit. Accordingly, the assailed Decision and Resolution are hereby **AFFIRMED**.

SO ORDERED.

ERNESTO D. ACOSTA
Presiding Justice

WE CONCUR:

JUANITO C. CASTANEDA, JR.
Associate Justice

LOVELL R. BAUTISTA
Associate Justice

ERLINDA P. UY
Associate Justice

CAESAR A. CASANOVA
Associate Justice

OLGA PALANCA-ENRIQUEZ
Associate Justice

CERTIFICATION

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

ERNESTO D. ACOSTA
Presiding Justice
Chairman, First Division

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