626 Phil. 566

THIRD DIVISION

[G.R. No. 180356, February 16, 2010]

SOUTH AFRICAN AIRWAYS, PETITIONER, VS. COMMISSIONER OF INTERNAL REVENUE, RESPONDENT.

D E C I S I O N

VELASCO JR., J.:

The Case

This Petition for Review on Certiorari under Rule 45 seeks the reversal of the July 19, 2007 Decision[1] and October 30, 2007 Resolution[2] of the Court of Tax Appeals (CTA) *En Banc* in CTA E.B. Case No. 210, entitled *South African Airways v. Commissioner of Internal Revenue*. The assailed decision affirmed the Decision dated May 10, 2006[3] and Resolution dated August 11, 2006[4] rendered by the CTA First Division.

The Facts

Petitioner South African Airways is a foreign corporation organized and existing under and by virtue of the laws of the Republic of South Africa. Its principal office is located at Airways Park, Jones Road, Johannesburg International Airport, South Africa. In the Philippines, it is an internal air carrier having no landing rights in the country. Petitioner has a general sales agent in the Philippines, Aerotel Limited Corporation (Aerotel). Aerotel sells passage documents for compensation or commission for petitioner's off-line flights for the carriage of passengers and cargo between ports or points outside the territorial jurisdiction of the Philippines. Petitioner is not registered with the Securities and Exchange Commission as a corporation, branch office, or partnership. It is not licensed to do business in the Philippines.

For the taxable year 2000, petitioner filed separate quarterly and annual income tax returns for its off-line flights, summarized as follows:

	Period	Date Filed		2.5% Gross Phil. Billings
For Passenger	1st Quarter	May 30, 2000 August 29, 2000	PhP	222,531.25 424,046.95

	2nd Quarter 3rd Quarter 4th Quarter	November 29, 2000 April 16, 2000		422,466.00 453,182.91
Sub-total			PhP	1,522,227.11
For Cargo	1st Quarter 2nd Quarter 3rd Quarter 4th Quarter	May 30, 2000 August 29, 2000 November 29, 2000 April 16, 2000	PhP	81,531.00 50,169.65 36,383.74 37,454.88
Sub-total			PhP	205,539.27
TOTAL				1,727,766.38

Thereafter, on February 5, 2003, petitioner filed with the Bureau of Internal Revenue, Revenue District Office No. 47, a claim for the refund of the amount of PhP 1,727,766.38 as erroneously paid tax on Gross Philippine Billings (GPB) for the taxable year 2000. Such claim was unheeded. Thus, on April 14, 2003, petitioner filed a Petition for Review with the CTA for the refund of the abovementioned amount. The case was docketed as CTA Case No. 6656.

On May 10, 2006, the CTA First Division issued a Decision denying the petition for lack of merit. The CTA ruled that petitioner is a resident foreign corporation engaged in trade or business in the Philippines. It further ruled that petitioner was not liable to pay tax on its GPB under Section 28(A)(3)(a) of the National Internal Revenue Code (NIRC) of 1997. The CTA, however, stated that petitioner is liable to pay a tax of 32% on its income derived from the sales of passage documents in the Philippines. On this ground, the CTA denied petitioner's claim for a refund.

Petitioner's Motion for Reconsideration of the above decision was denied by the CTA First Division in a Resolution dated August 11, 2006.

Thus, petitioner filed a Petition for Review before the CTA *En Banc*, reiterating its claim for a refund of its tax payment on its GPB. This was denied by the CTA in its assailed decision. A subsequent Motion for Reconsideration by petitioner was also denied in the assailed resolution of the CTA *En Banc*.

Hence, petitioner went to us.

The Issues

> Whether or not petitioner, as an off-line international carrier selling passage documents through an independent sales agent in the Philippines, is engaged in trade or business in the Philippines subject to the 32% income tax imposed by

> Section 28 (A)(1) of the 1997 NIRC.
>
> Whether or not the income derived by petitioner from the sale of passage documents covering petitioner's off-line flights is Philippine-source income subject to Philippine income tax.
>
> Whether or not petitioner is entitled to a refund or a tax credit of erroneously paid tax on Gross Philippine Billings for the taxable year 2000 in the amount of P1,727,766.38.[5]

The Court's Ruling

This petition must be denied.

Petitioner Is Subject to Income Tax at the Rate of 32% of Its Taxable Income

Preliminarily, we emphasize that petitioner is claiming that it is exempted from being taxed for its sale of passage documents in the Philippines. Petitioner, however, failed to sufficiently prove such contention.

In *Commissioner of Internal Revenue v. Acesite (Philippines) Hotel Corporation*,[6] we held, "Since an action for a tax refund partakes of the nature of an exemption, which cannot be allowed unless granted in the most explicit and categorical language, it is strictly construed against the claimant who must discharge such burden convincingly."

Petitioner has failed to overcome such burden.

In essence, petitioner calls upon this Court to determine the legal implication of the amendment to Sec. 28(A)(3)(a) of the 1997 NIRC defining GPB. It is petitioner's contention that, with the new definition of GPB, it is no longer liable under Sec. 28(A)(3)(a). Further, petitioner argues that because the 2 1/2% tax on GPB is inapplicable to it, it is thereby excluded from the imposition of any income tax.

Sec. 28(b)(2) of the 1939 NIRC provided:

> (2) Resident Corporations. - A corporation organized, authorized, or existing under the laws of a foreign country, engaged in trade or business within the Philippines, shall be taxable as provided in subsection (a) of this section upon the total net income received in the preceding taxable year from all sources within the Philippines: *Provided*, *however*, that international carriers shall pay a tax of two and one-half percent on their gross Philippine billings.

This provision was later amended by Sec. 24(B)(2) of the 1977 NIRC, which defined GPB as follows:

> "Gross Philippine billings" include gross revenue realized from uplifts anywhere in the world by any international carrier doing business in the Philippines of passage documents sold therein, whether for passenger, excess baggage or mail, provided the cargo or mail originates from the Philippines.

In the 1986 and 1993 NIRCs, the definition of GPB was further changed to read:

> "Gross Philippine Billings" means gross revenue realized from uplifts of passengers anywhere in the world and excess baggage, cargo and mail originating from the Philippines, covered by passage documents sold in the Philippines.

Essentially, prior to the 1997 NIRC, GPB referred to revenues from uplifts anywhere in the world, provided that the passage documents were sold in the Philippines. Legislature departed from such concept in the 1997 NIRC where GPB is now defined under Sec. 28(A)(3)(a):

> "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.

Now, it is the place of sale that is irrelevant; as long as the uplifts of passengers and cargo occur to or from the Philippines, income is included in GPB.

As correctly pointed out by petitioner, inasmuch as it does not maintain flights to or from the Philippines, it is not taxable under Sec. 28(A)(3)(a) of the 1997 NIRC. This much was also found by the CTA. But petitioner further posits the view that due to the non-applicability of Sec. 28(A)(3)(a) to it, it is precluded from paying any other income tax for its sale of passage documents in the Philippines.

Such position is untenable.

In *Commissioner of Internal Revenue v. British Overseas Airways Corporation* (*British Overseas Airways*),[7] which was decided under similar factual circumstances, this Court ruled that off-line air carriers having general sales agents in the Philippines are engaged in or doing business in the Philippines and that their income from sales of passage documents here is income from within the Philippines. Thus, in that case, we held the off-line air carrier liable for the 32% tax on its taxable income.

Petitioner argues, however, that because *British Overseas Airways* was decided under the 1939 NIRC, it does not apply to the instant case, which must be decided under the 1997 NIRC. Petitioner alleges that the 1939 NIRC taxes resident foreign corporations, such as itself, on all income from sources within the Philippines. Petitioner's interpretation of Sec. 28(A)(3)(a) of the 1997 NIRC is that, since it is an international carrier that does not maintain flights to or from the Philippines, thereby having no GPB as defined, it is exempt from paying any income tax at all. In other words, the existence of Sec. 28(A)(3)(a) according to petitioner precludes the application of Sec. 28(A)(1) to it.

Its argument has no merit.

First, the difference cited by petitioner between the 1939 and 1997 NIRCs with regard to the taxation of off-line air carriers is more apparent than real.

We point out that Sec. 28(A)(3)(a) of the 1997 NIRC does not, in any categorical term, exempt all international air carriers from the coverage of Sec. 28(A)(1) of the 1997 NIRC. Certainly, had legislature's intentions been to completely exclude all international air carriers from the application of the general rule under Sec. 28(A)(1), it would have used the appropriate language to do so; but the legislature did not. Thus, the logical interpretation of such provisions is that, if Sec. 28(A)(3)(a) is applicable to a taxpayer, then the general rule under Sec. 28(A)(1) would not apply. If, however, Sec. 28(A)(3)(a) does not apply, a resident foreign corporation, whether an international air carrier or not, would be liable for the tax under Sec. 28(A)(1).

Clearly, no difference exists between *British Overseas Airways* and the instant case, wherein petitioner claims that the former case does not apply. Thus, *British Overseas Airways* applies to the instant case. The findings therein that an off-line air carrier is doing business in the Philippines and that income from the sale of passage documents here is Philippine-source income must be upheld.

Petitioner further reiterates its argument that the intention of Congress in amending the definition of GPB is to exempt off-line air carriers from income tax by citing the pronouncements made by Senator Juan Ponce Enrile during the deliberations on the provisions of the 1997 NIRC. Such pronouncements, however, are not controlling on this Court. We said in *Espino v. Cleofe*:[8]

> A cardinal rule in the interpretation of statutes is that the meaning and intention of the law-making body must be sought, first of all, in the words of the statute itself, read and considered in their natural, ordinary, commonly-accepted and most obvious significations, according to good and approved usage and without

resorting to forced or subtle construction. Courts, therefore, as a rule, cannot presume that the law-making body does not know the meaning of words and rules of grammar. Consequently, the grammatical reading of a statute must be presumed to yield its correct sense. x x x **It is also a well-settled doctrine in this jurisdiction that statements made by individual members of Congress in the consideration of a bill do not necessarily reflect the sense of that body and are, consequently, not controlling in the interpretation of law.** (Emphasis supplied.)

Moreover, an examination of the subject provisions of the law would show that petitioner's interpretation of those provisions is erroneous.

Sec. 28(A)(1) and (A)(3)(a) provides:

SEC. 28. Rates of Income Tax on Foreign Corporations. -

(A) Tax on Resident Foreign Corporations. -

(1) In General. - Except as otherwise provided in this Code, a corporation organized, authorized, or existing under the laws of any foreign country, engaged in trade or business within the Philippines, shall be subject to an income tax equivalent to thirty-five percent (35%) of the taxable income derived in the preceding taxable year from all sources within 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%).

x x x x

(3) International Carrier. - An international carrier doing business in the Philippines shall pay a tax of two and one-half percent (2 1/2%) 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.

Sec. 28(A)(1) of the 1997 NIRC is a general rule that resident foreign corporations are liable for 32% tax on all income from sources within the Philippines. Sec. 28(A)(3) is an exception to this general rule.

An exception is defined as "that which would otherwise be included in the provision from which it is excepted. It is a clause which exempts something from the operation of a statue by express words."[9] Further, "an exception need not be introduced by the words `except' or `unless.' An exception will be construed as such if it removes something from the operation of a provision of law."[10]

In the instant case, the general rule is that resident foreign corporations shall be liable for a 32% income tax on their income from within the Philippines, except for resident foreign corporations that are international carriers that derive income "from carriage of persons, excess baggage, cargo and mail originating from the Philippines" which shall be taxed at 2 1/2% of their Gross Philippine Billings. Petitioner, being an international carrier with no flights originating from the Philippines, does not fall under the exception. As such, petitioner must fall under the general rule. This principle is embodied in the Latin maxim, *exception firmat regulam in casibus non exceptis*, which means, a thing not being excepted must be regarded as coming within the purview of the general rule.[11]

To reiterate, the correct interpretation of the above provisions is that, if an international air carrier maintains flights to and from the Philippines, it shall be taxed at the rate of 2 1/2% of its Gross Philippine Billings, while international air carriers that do not have flights to and from the Philippines but nonetheless earn income from other activities in the country will be taxed at the rate of 32% of such income.

As to the denial of petitioner's claim for refund, the CTA denied the claim on the basis that petitioner is liable for income tax under Sec. 28(A)(1) of the 1997 NIRC. Thus, petitioner raises the issue of whether the existence of such liability would preclude their claim for a refund of tax paid on the basis of Sec. 28(A)(3)(a). In answer to petitioner's motion for reconsideration, the CTA First Division ruled in its Resolution dated August 11, 2006, thus:

> On the fourth argument, petitioner avers that a deficiency tax assessment does not, in any way, disqualify a taxpayer from claiming a tax refund since a refund claim can proceed independently of a tax assessment and that the assessment

> cannot be offset by its claim for refund.
>
> Petitioner's argument is erroneous. Petitioner premises its argument on the existence of an assessment. In the assailed Decision, this Court did not, in any way, assess petitioner of any deficiency corporate income tax. The power to make assessments against taxpayers is lodged with the respondent. For an assessment to be made, respondent must observe the formalities provided in Revenue Regulations No. 12-99. This Court merely pointed out that petitioner is liable for the regular corporate income tax by virtue of Section 28(A)(3) of the Tax Code. Thus, there is no assessment to speak of.[12]

Precisely, petitioner questions the offsetting of its payment of the tax under Sec. 28(A)(3)(a) with their liability under Sec. 28(A)(1), considering that there has not yet been any assessment of their obligation under the latter provision. Petitioner argues that such offsetting is in the nature of legal compensation, which cannot be applied under the circumstances present in this case.

Article 1279 of the Civil Code contains the elements of legal compensation, to wit:

> Art. 1279. In order that compensation may be proper, it is necessary:
>
> (1) That each one of the obligors be bound principally, and that he be at the same time a principal creditor of the other;
>
> (2) That both debts consist in a sum of money, or if the things due are consumable, they be of the same kind, and also of the same quality if the latter has been stated;
>
> (3) That the two debts be due;
>
> (4) That they be liquidated and demandable;
>
> (5) That over neither of them there be any retention or controversy, commenced by third persons and communicated in due time to the debtor.

And we ruled in *Philex Mining Corporation v. Commissioner of Internal Revenue*,[13] thus:

> In several instances prior to the instant case, we have already made the pronouncement that taxes cannot be subject to compensation for the simple reason that the government and the taxpayer are not creditors and debtors of each other. There is a material distinction between a tax and debt. Debts are due

to the Government in its corporate capacity, while taxes are due to the Government in its sovereign capacity. We find no cogent reason to deviate from the aforementioned distinction.

Prescinding from this premise, in *Francia v. Intermediate Appellate Court*, we categorically held that taxes cannot be subject to set-off or compensation, thus:

> We have consistently ruled that there can be no off-setting of taxes against the claims that the taxpayer may have against the government. A person cannot refuse to pay a tax on the ground that the government owes him an amount equal to or greater than the tax being collected. The collection of a tax cannot await the results of a lawsuit against the government.

The ruling in *Francia* has been applied to the subsequent case of *Caltex Philippines, Inc. v. Commission on Audit*, which reiterated that:

> . . . a taxpayer may not offset taxes due from the claims that he may have against the government. Taxes cannot be the subject of compensation because the government and taxpayer are not mutually creditors and debtors of each other and a claim for taxes is not such a debt, demand, contract or judgment as is allowed to be set-off.

Verily, petitioner's argument is correct that the offsetting of its tax refund with its alleged tax deficiency is unavailing under Art. 1279 of the Civil Code.

Commissioner of Internal Revenue v. Court of Tax Appeals,[14] however, granted the offsetting of a tax refund with a tax deficiency in this wise:

> Further, it is also worth noting that the Court of Tax Appeals erred in denying petitioner's supplemental motion for reconsideration alleging bringing to said court's attention the existence of the deficiency income and business tax assessment against Citytrust. The fact of such deficiency assessment is intimately related to and inextricably intertwined with the right of respondent bank to claim for a tax refund for the same year. To award such refund despite the existence of that deficiency assessment is an absurdity and a polarity in conceptual effects. Herein private respondent cannot be entitled to refund and at the same time be liable for a tax deficiency assessment for the same year.
>
> **The grant of a refund is founded on the assumption that the tax return is valid, that is, the facts stated therein are true and correct. The deficiency**

assessment, although not yet final, created a doubt as to and constitutes a challenge against the truth and accuracy of the facts stated in said return which, by itself and without unquestionable evidence, cannot be the basis for the grant of the refund.

Section 82, Chapter IX of the National Internal Revenue Code of 1977, which was the applicable law when the claim of Citytrust was filed, provides that "(w)hen an assessment is made in case of any list, statement, or return, which in the opinion of the Commissioner of Internal Revenue was false or fraudulent or contained any understatement or undervaluation, no tax collected under such assessment shall be recovered by any suits unless it is proved that the said list, statement, or return was not false nor fraudulent and did not contain any understatement or undervaluation; but this provision shall not apply to statements or returns made or to be made in good faith regarding annual depreciation of oil or gas wells and mines."

Moreover, to grant the refund without determination of the proper assessment and the tax due would inevitably result in multiplicity of proceedings or suits. If the deficiency assessment should subsequently be upheld, the Government will be forced to institute anew a proceeding for the recovery of erroneously refunded taxes which recourse must be filed within the prescriptive period of ten years after discovery of the falsity, fraud or omission in the false or fraudulent return involved. This would necessarily require and entail additional efforts and expenses on the part of the Government, impose a burden on and a drain of government funds, and impede or delay the collection of much-needed revenue for governmental operations.

Thus, to avoid multiplicity of suits and unnecessary difficulties or expenses, it is both logically necessary and legally appropriate that the issue of the deficiency tax assessment against Citytrust be resolved jointly with its claim for tax refund, to determine once and for all in a single proceeding the true and correct amount of tax due or refundable.

In fact, as the Court of Tax Appeals itself has heretofore conceded, it would be only just and fair that the taxpayer and the Government alike be given equal opportunities to avail of remedies under the law to defeat each other's claim and to determine all matters of dispute between them in one single case. It is important to note that in determining whether or not petitioner is entitled to the refund of the amount paid, it would [be] necessary to determine how much the Government is entitled to collect as taxes. This would necessarily include the determination of the correct liability of the taxpayer and, certainly, a determination of this case would constitute res judicata on both parties as to all the matters subject thereof or necessarily involved therein. (Emphasis supplied.)

Sec. 82, Chapter IX of the 1977 Tax Code is now Sec. 72, Chapter XI of the 1997 NIRC. The above pronouncements are, therefore, still applicable today.

Here, petitioner's similar tax refund claim assumes that the tax return that it filed was correct. Given, however, the finding of the CTA that petitioner, although not liable under Sec. 28(A)(3)(a) of the 1997 NIRC, is liable under Sec. 28(A)(1), the correctness of the return filed by petitioner is now put in doubt. As such, we cannot grant the prayer for a refund.

Be that as it may, this Court is unable to affirm the assailed decision and resolution of the CTA *En Banc* on the outright denial of petitioner's claim for a refund. Even though petitioner is not entitled to a refund due to the question on the propriety of petitioner's tax return subject of the instant controversy, it would not be proper to deny such claim without making a determination of petitioner's liability under Sec. 28(A)(1).

It must be remembered that the tax under Sec. 28(A)(3)(a) is based on GPB, while Sec. 28(A)(1) is based on taxable income, that is, gross income less deductions and exemptions, if any. It cannot be assumed that petitioner's liabilities under the two provisions would be the same. There is a need to make a determination of petitioner's liability under Sec. 28(A)(1) to establish whether a tax refund is forthcoming or that a tax deficiency exists. The assailed decision fails to mention having computed for the tax due under Sec. 28(A)(1) and the records are bereft of any evidence sufficient to establish petitioner's taxable income. There is a necessity to receive evidence to establish such amount vis-à-vis the claim for refund. It is only after such amount is established that a tax refund or deficiency may be correctly pronounced.

WHEREFORE, the assailed July 19, 2007 Decision and October 30, 2007 Resolution of the CTA *En Banc* in CTA E.B. Case No. 210 are **SET ASIDE**. The instant case is **REMANDED** to the CTA *En Banc* for further proceedings and appropriate action, more particularly, the reception of evidence for both parties and the corresponding disposition of CTA E.B. Case No. 210 not otherwise inconsistent with our judgment in this Decision.

SO ORDERED.

Corona, (Chairperson), Leonardo-De Castro[*], *Peralta,* and *Mendoza, JJ.*, concur.

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[*] Additional member per raffle dated February 3, 2010.

[1] *Rollo*, pp. 68-79. Penned by Associate Justice Erlinda P. Uy and concurred in by Presiding Justice Ernesto D. Acosta and Associate Justices Lovell R. Bautista and Olga Palanca-Enriquez.

[2] Id. at 126-127.

[3] Id. at 339-347.

[4] Id. at 367-373.

[5] Id. at 11.

[6] G.R. No. 147295, February 16, 2007, 516 SCRA 93, 103.

[7] No. L-65773-74, April 30, 1987, 149 SCRA 395.

[8] No. L-33410, July 13, 1973, 52 SCRA 92, 98.

[9] R. Agpalo, STATUTORY CONSTRUCTION 241 (4th ed., 1998).

[10] Id. at 242.

[11] Id.

[12] *Rollo*, p. 372.

[13] G.R. No. 125704, August 28, 1998, 294 SCRA 687, 695-696.

[14] G.R. No. 106611, July 21, 1994, 234 SCRA 348, 356-358.