

COMMISSIONER OF INTERNAL REVENUE, PETITIONER, VS. ROYAL INTEROCEAN LINES AND THE COURT OF TAX APPEALS, RESPONDENTS.

G.R. No. L-26806. July 30, 1970

Ponente: CONCEPCION, C.J.

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CONCEPCION, C.J.:

Appeal by the Commissioner of Internal Revenue from a decision of the Court of Tax Appeals reversing that of said official, in connection with the liability of the Royal Interocean Lines, Inc., for deficiency carrier's percentage tax, plus surcharge.

Said Royal Interocean Lines, Inc. - hereinafter referred to as the taxpayer - is a foreign corporation duly licensed to do business in the Philippines, with head office in Amsterdam, Holland. The taxpayer is engaged in the operation of ocean-going vessels, plying between the Philippines and other countries, transporting passengers and cargo. It is, likewise, an agent and representative of the Holland East Asia Lines, a Dutch shipping company, from which the taxpayer receives compensation in the form of commissions for services rendered. It is not disputed that from February to May, 1962, inclusive, vessels of the taxpayer and/or the Holland East Asia Lines called at Philippine ports to load cargo, with freight, payable at destination, valued at US \$37,501.50. This sum had been collected by and paid to the taxpayer's head office in Holland, and was not actually turned over or forwarded, as such freight fees, to the taxpayer in the Philippines. The only remittances received by the latter from its aforementioned head office were those made, through its agent bank, for the operational expenses of the branch office in the Philippines.

Prior to January, 1962, its dollar earnings derived from freight revenues were converted into the Philippine peso equivalent thereof, under the prevailing free market rate, for purposes of the common carrier's tax prescribed in Section 192 of the National Internal Revenue Code. Thereafter, the taxpayer discontinued this practice and, since February, 1962, it reported said revenues, in its monthly returns for carrier's tax, based on the parity rate of P2 to \$1, and paid P1,500.00 as such carrier's tax. Upon examination of the records of the taxpayer, the Commissioner of Internal Revenue, hereinafter referred to as the petitioner, held that, applying the free market conversion rate, the taxpayer's gross receipts from February to, May, 1962, aggregated P163,776.38, and, based thereon, demanded payment of P2,219.35 as deficiency common carrier's tax, plus surcharge and penalty. Having found, soon later, that the sum of P29,920.50 had twice been included in the computation of said receipts, petitioner subsequently agreed with the taxpayer that its gross receipts for the period in question, reckoned on the free market conversion rate, amounted to P133,855.88, based on which petitioner demanded, in a letter received by the taxpayer on January 18, 1963, payment of the total sum of P1,471.39, consisting of P1,177.12, as deficiency carrier's tax, plus a 25% surcharge, computed as follows:

Total gross receipts (\$37,501.50, U.S.

currency) converted to Philippine

"x x x x

"(m) Any other transactions involving international financial implications."2

Subdivision (h) of said section 2 of Circular No. 42 was amended on May 27, 1957, to read as follows:

"(h) All collections of residents made abroad thru their overseas branch office, agents or representatives. Such collections shall be brought or ordered to be brought by such residents into the Philippines in U.S. currency or in any other currency acceptable to the Central Bank."3

Pursuant to this provision, the aforementioned freight fees earned by the taxpayer are the product of "foreign exchange" transactions, within the purview of Central Bank Circular No. 20, because, having been collected by the taxpayer's main office in Amsterdam, said fees are deemed to have been paid to the taxpayer in the Philippines, on behalf of which the former had acted; because they were due for services rendered in the Philippines, without which said main office would have had no right to collect or receive said fees; because the same represented the compensation for services performed by a resident of the Philippines - the taxpayer's branch office therein; because they represented "collections of residents made abroad," to which subdivision (h) of said section 2 refers; and because they fall under the category of "(a)ny other transactions involving international financial implications," covered by subdivision (m) of the same section.

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 P3.47 to P3.65 to a US dollar, at which rates 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.

The theory of the taxpayer to the effect that, not having been physically remitted to the Philippines, the fees in question do not partake of the nature of revenues derived from foreign exchange transactions, is manifestly devoid of merit. The transactions from which said revenues were derived involved the loading of cargo in the Philippines, the transportation of said cargo to its ports of destination, the delivery of the cargo to the respective consignees, and the payment of the corresponding fees to the taxpayer's head office at Amsterdam. As regards the taxpayer, the transactions were consummated upon delivery of the cargo to the consignee. Upon the other hand, the obligations of the latter or the shipper were discharged upon payment of the freight. Insofar as the parties to said transaction were concerned, the same were fully completed upon payment of the fees at Amsterdam. The question whether or not such fees were to be remitted by the taxpayer's head office in that City to its branch office in the Philippines, which had earned it, was one that concerned exclusively the former and the latter, it being independent of the rights and obligations of the parties to the aforementioned transactions, which were extinguished upon delivery of the cargo at destination and payment of the freight to said main office of the taxpayer. In short, the remittance or non-remittance of said fees could not affect the nature of said transactions, as involving foreign exchange, not being a part thereof in any manner whatsoever.

Then again, we take it that - in line with the ordinary course of business, adherence to which is presumed, in the absence of proof to the contrary - upon receipt of said freight, the same must have been credited in the records of the taxpayer's main office in Amsterdam, in favor of its branch office in the Philippines, and that, upon notice of such payment to the head office in Amsterdam, the branch office in the Philippines must have, in turn, debited

said fees against its main office. Such processes of bookkeeping and accounting are, for legal purposes, tantamount to delivery, receipt, or remittance. In fact, by so crediting said fees, the taxpayer's main office in Amsterdam in effect acknowledged being, in a way, indebted to its Philippine branch, as debited in the latter's records, in much the same way as the former would have been had it received the fees directly from the latter. Incidentally, this is in accord with established practice especially among merchants the world over, who seldom bring or send money physically from one country to another, but, generally, resort to bills, notes or other conventional forms of transacting business in the manner they may deem most practical and suitable to their respective interests.

Needless to say, the remittances made by the taxpayer's head office to its Philippine branch, for the operational expenses thereof - or for any other purposes - must have been credited in the books of account of the latter in favor of the former, in the records of which they must have been debited against said branch, and, hence, deducted from its assets in Amsterdam, including the freight revenues involved herein.

The infirmity of the taxpayer's theory becomes readily apparent when we consider that, if upheld, its effect would be to subject to the carrier's tax at the free market rate all business enterprises that bring their dollar earnings into the Philippines, and to exempt from such tax or, apply the parity rate to those who do not bring in their dollars or other foreign exchange, thereby discriminating against those who help maintain or increase our international reserve and in favor of those who do not only fail to do so, but jeopardize the condition of such reserve, by keeping abroad their dollar and other earnings, and, worse still, by inducing other merchants in the Philippines, engaged in a foreign trade, to adopt the same practice, in order to avoid, evade or cut down the payment of said tax. This result could not surely have been intended or countenanced by the framers of our tax laws, much less by those responsible for our policy of control and, later, of gradual decontrol, considering their grave concern for our international reserve and the stability of the Philippine currency.

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 P2 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. Although the decision in the case cited contains a phrase suggesting that there can be no foreign exchange operation when the amount involved therein is not remitted to the Philippines, this implied pronouncement was a mere obiter, inasmuch as the result would have been the same had there been a remittance of said amount, there being, at that time, no other legal rate of exchange for US dollars than the parity rate.

It is, thus, our considered view that the freight revenues accruing to the taxpayer in the present case, even though collected abroad and not remitted to its branch office in the Philippines, are part of its foreign exchange operations and subject to the common carrier's tax, computed at the free market rate then prevailing.

It is next urged that the 25% surcharge sought to be collected by the petitioner should not be imposed upon the taxpayer, it having acted in good faith in doing what it did, for it merely followed the advice of counsel. The aforementioned surcharge was imposed by petitioner herein in accordance with Section 183 of the National Internal Revenue Code,⁴ subdivision (a) of which reads:

"SEC. 183. Payment of percentage taxes - (a) In general.- It shall be the duty of every person conducting a business on which a percentage tax is imposed under this Title, to make a true and complete return of the amount of his, her or its gross monthly sales, receipts or earnings, or gross value of output actually removed

from the factory or mill warehouse and within twenty days after the end of each month, pay the tax due thereon: Provided, That any person retiring from a business subject to the percentage tax shall notify the nearest internal revenue officer thereof, file his return or declaration, and pay the tax due thereon within twenty days after closing his business.

"If the percentage tax on any business is not paid within the time specified above, the amount of the tax shall be increased by twenty-five per centum, the increment to be a part of the tax.

"In case of willful neglect to file the return within the period prescribed herein, or in case a false or fraudulent return is willfully made, there shall be added to the tax or to the deficiency tax, in case any payment has been made on the basis of such return before the discovery of the falsity, or fraud, a surcharge of fifty per centum of its amount. The amount so added to any tax shall be collected at the same time and in the same manner and as part of the tax unless the tax has been paid before the discovery of the falsity or fraud, in which case the amount so added shall be collected in the same manner as the tax."⁵

Pursuant to this provision, if the tax in question is not paid "within twenty days after the end of each month, x x x the amount of the tax shall be increased by twenty-five per centum, the increment to be a part of the tax." As early as February 11, 1925, We held in *Lim Co Chui v. Posadas*,⁶ construing a similar provision, that the same is "mandatory," and, accordingly, sanctioned the imposition of the 25% surcharge on the sales tax involved therein, which had been paid one day late, or October 21, 1924, because of a riot against the Chinese in Manila on October 18, 19 and 20, 1924. This view was reiterated in *Koppel (Phil.) Inc. v. Collector of Internal Revenue*,⁷ referring to a similar tax payable not later than January 20, 1942, but not paid then, owing to the outbreak of war in the Pacific and the military occupation of the Philippines by Japanese forces. To the same effect are *Insular Lumber Co. v. Collector of Internal Revenue*,⁸ *Republic of the Philippines v. Luzon Industrial Corp.*⁹ - in which a check, issued on time and brought by a messenger to the office of the City Treasurer on April 20, 1948, could not be delivered to him on that date, on account of the numerous taxpayers then lined up in his office, and was not actually received by said official until April 22, 1948 - *Pirovano v. Commissioner of Internal Revenue*¹⁰ and *Republic of the Philippines v. Lim Tian Teng Sons & Co., Inc.*¹¹

*Connel Bros. Co v. Collector of Internal Revenue*¹² and *Imus Electric Co. v. Court of Tax Appeals*,¹³ upon which the taxpayer relies, are not in point.

In the first case, the issue was whether the sales tax of 5% of the "gross selling price" of certain articles shall be imposed upon the price set forth in the corresponding invoices, notwithstanding the fact that the phrase "5% sales tax included" appeared thereon. The question was resolved in the affirmative, upon the ground that a circular of the Bureau of Internal Revenue, implementing the law imposing said tax, provided:

"x x x Unless billed to the purchaser as separate items in the invoice, the amounts intended to cover the sales tax shall be considered as part of the gross selling price of the articles sold, and deductions thereof will not be allowed."

and that the taxpayer had not complied with it since January 18, 1948, - although it had adhered thereto up to then, by issuing invoices containing an itemization of the actual selling price and of the 5% sales tax thereon, which was added to the selling price and shifted to the customer, who paid the total amount.

It should be noted, however, that - unlike the taxpayer in the case at bar, which declared its revenues from February to May 1962 as P75,003.00, when, in fact, the revenues aggregated P133,855.88 - *Connel Bros. Co.* had set forth in its invoices the true amounts collected from its customers, and the issue hinged merely on the application of the law thereto, namely, whether the sales tax shall be based upon said amounts, or should be computed after deducting therefrom the sum corresponding to the tax. Moreover, although disagreeing with the position taken by the Bureau of Internal Revenue, *Connel Bros.* had forthwith deposited the amount assessed by

the same, and the deposit was later converted into payment, followed by a formal request for refund and then, upon denial thereof, by the corresponding petition for review in the Court of Tax appeals. Thus, upon demand, the amount representing the taxes sought to be collected by the Government was placed at the latter's disposal, subject only to the taxpayer's claim that it was not legally due. Hence, the reason for the imposition of a surcharge - which is non-payment within the period prescribed by law - did not, in effect, exist in *Connel Bros.*' case.

The second case initially referred to a similar claim for refund of payments made of the corporate franchise tax - provided in section 259 of the Tax Code, as amended by Rep. Act No. 39, effective in 1946 - of 5% of the gross earnings or receipts of a corporation that had, since 1930, a municipal franchise imposing a tax of 1% of the earnings for the first 20 years and 2% for the next 15 years. The taxpayer maintained that the application of the Tax Code impaired its vested rights under said municipal franchise. The claim for refund had started an exchange of views, between the Bureau of Internal Revenue and the taxpayer, that dragged for a number of years, culminating, in September 1961, in an assessment for deficiency franchise tax, for the period from January 1956 to September 1960, plus 25% surcharge. Although the claim of impairment of contractual obligation was overruled, for the reason that the municipal franchise contained an express reservation that it was subject to amendment or repeal, We exempted the taxpayer from the payment of the surcharge upon the authority of the *Connel Bros.*' case.

Regardless of our present opinion on the applicability to the *Imus* case of the view taken in the *Connel Bros.*' case concerning the payment of surcharges, the fact is that, in such case, there had been no failure to pay the tax assessed therein, so that there really was no legal justification for the imposition of surcharges. The circumstance that *Imus Electric Co.* had begun by demanding a refund of the payments it had made, for the period from 1948 to 1951, pursuant to the Tax Code, to which, it later claimed, it could not be made subject without violating rights vested under its municipal franchise, may, perhaps, account for the reliance upon the *Connel Bros.*' case, although the issue between the electric company and the Government, eventually, became one for collection of the deficiency franchise tax from 1956 to 1960.

At any rate, neither case nor both suffice to outweigh the above-mentioned six cases declaring that the provision imposing surcharges is mandatory. The alleged good faith of the taxpayer herein is - apart from being insufficient to justify a departure from the rule laid down and repeatedly applied in said cases - merely based upon the advice said to have been given by its counsel. Considering, moreover, that, up to December, 1961, the taxpayer had reported its earnings at the free market conversion rate - thereby indicating that such was, in its belief, the rate at which its foreign exchange transactions should be computed - its change of policy in 1962, allegedly following said advice of counsel, implied no more than the taking of a calculated risk.

WHEREFORE, the appealed decision of the Court of Tax Appeals is reversed, and judgment shall be entered affirming that of the Commissioner of Internal Revenue, except as to the compromise penalty of P200.00, which is hereby eliminated, and sentencing respondent corporation, *Royal Interocean Lines, Inc.*, to pay to petitioner herein the sum of P1,471.39, with interest thereon at the legal rate from January 18, 1963, when it received the letter of demand of said petitioner, until full payment,¹⁴ with costs against said respondent.

SO ORDERED.

Reyes, J.B.L., Dizon, Makalintal, Zaldivar, Castro, Fernando, Teehankee, Barredo, and Villamor, JJ., concur.

1 G.R. No. L-16850, May 30, 1962.

2 Underscoring supplied.

3 Underscoring supplied.

4 Commonwealth Act No. 466, as amended by Rep. Act No. 2025, approved on June 22, 1957.

5 Underscoring supplied.

6 47 Phil. 460, 462.

7 87 Phil. 348, 350-351.

8 98 Phil. 1012-1013.

9 102 Phil. 189, 193.

10 L-19865, July 31, 1965.

11 L-21731, March 31, 1966.

12 L-15470, Dec. 26, 1963.

13 L-22421, March 18, 1967.

14 Art. 2209, Civil Code of the Philippines; Commissioner of Internal Revenue v. Abad, L-19627, June 27, 1968.

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