

SECOND DIVISION

[G.R. No. 167260, February 27, 2009]

**THE CITY OF ILOILO, MR. ROMEO V. MANIKAN, IN HIS
CAPACITY AS THE TREASURER OF ILOILO CITY, PETITIONERS,
VS. SMART COMMUNICATIONS, INC. (SMART), RESPONDENT.**

DECISION

BRION, J.:

Before this Court is the appeal by *certiorari* filed by the City of Iloilo (*petitioner*) under Rule 45 of the Rules of Court seeking to set aside the decision of the Regional Trial Court (*RTC*) of Iloilo City, Branch 28, which declared that respondent SMART Communications, Inc. (*SMART*) is exempt from the payment of local franchise and business taxes.

BACKGROUND FACTS

The facts of the case are not in dispute. SMART received a letter of assessment dated February 12, 2002 from petitioner requiring it to pay deficiency local franchise and business taxes (in the amount of P764,545.29, plus interests and surcharges) which it incurred for the years 1997 to 2001. SMART protested the assessment by sending a letter dated February 15, 2002 to the City Treasurer. It claimed exemption from payment of local franchise and business taxes based on Section 9 of its legislative franchise under Republic Act (*R.A.*) No. 7294 (*SMART's franchise*). Under SMART's franchise, it was required to pay a franchise tax equivalent to 3% of all gross receipts, which amount shall be in lieu of all taxes. SMART contends that the "in lieu of all taxes" clause covers local franchise and business taxes.

SMART similarly invoked R.A. No. 7925 or the Public Telecommunications Policy Act (*Public Telecoms Act*) whose Section 23 declares that any existing privilege, incentive, advantage, or exemption granted under existing franchises shall *ipso facto* become part of previously granted-telecommunications franchise. SMART contends that by virtue of Section 23, tax exemptions granted by the legislature to other holders of telecommunications franchise may be extended to and availed of by SMART.

Through a letter dated April 4, 2002, petitioner denied SMART's protest, citing the failure of SMART to comply with Section 252 of R.A. No. 7160 or the Local Government Code (*LGC*) before filing the protest against the assessment. Section 252 of the LGC requires payment of the tax before any protest against the tax assessment can be made.

SMART objected to the petitioner's denial of its protest by instituting a case against petitioner before the RTC of Iloilo City.^[1] The trial court ruled in favour of SMART and declared the telecommunications firm exempt from the payment of local franchise and business taxes;^[2] it agreed with SMART's claim of exemption under Section 9 of its franchise and Section 23 of the Public Telecoms Act.^[3]

From this judgment, petitioner files this petition for review on *certiorari* raising the sole issue of whether SMART is exempt from the payment of local franchise and business taxes.

THE COURT'S RULING

SMART relies on two provisions of law to support its claim for tax exemption: Section 9 of SMART's franchise and Section 23 of the Public Telecoms Act. After a review of pertinent laws and jurisprudence - particularly of *SMART Communications, Inc. v. City of Davao*,^[4] a case which, except for the respondent, involves the same set of facts and issues - we find SMART's claim for exemption to be unfounded. Consequently, we find the petition meritorious.

The basic principle in the construction of laws granting tax exemptions has been very stable. As early as 1916, in the case of *Government of the Philippine Islands v. Monte de Piedad*,^[5] this Court has declared that he who claims an exemption from his share of the common burden of taxation must justify his claim by showing that the Legislature intended to exempt him by words too plain to be beyond doubt or mistake. This doctrine was repeated in the 1926 case of *Asiatic Petroleum v. Llanes*,^[6] as well as in the case of *Borja v. Commissioner of Internal Revenue (CIR)*^[7] decided in 1961. Citing American jurisprudence, the Court stated in *E. Rodriguez, Inc. v. CIR*:^[8]

The right of taxation is inherent in the State. It is a prerogative essential to the perpetuity of the government; and he who claims an exemption from the common burden, must justify his claim by the clearest grant of organic or statute law xxx When exemption is claimed, it must be shown indubitably to exist. At the outset, every presumption is against it. A well-founded doubt is fatal to the claim; it is only when the terms of the concession are too explicit to admit fairly of any other construction that the proposition can be supported.

In the recent case of *Digital Telecommunications, Inc. v. City Government of Batangas, et al.*,^[9] we adhered to the same principle when we said:

A tax exemption cannot arise from vague inference...Tax exemptions must be clear and unequivocal. A taxpayer claiming a tax exemption must point to a specific provision of law conferring on the taxpayer, in clear and plain terms,

exemption from a common burden. Any doubt whether a tax exemption exists is resolved against the taxpayer.

The burden therefore is on SMART to prove that, based on its franchise and the Public Telecoms Act, it is entitled to exemption from the local franchise and business taxes being collected by the petitioner.

Claim for Exemption under SMART's franchise

Section 9 of SMART's franchise states:

Section 9. *Tax provisions.* -- The grantee, its successors or assigns shall be liable to pay the same taxes on their real estate buildings and personal property, exclusive of this franchise, as other persons or corporations which are now or hereafter may be required by law to pay. In addition thereto, **the grantee, its successors or assigns shall pay a franchise tax equivalent to three percent (3%) of all gross receipts of the business transacted under this franchise by the grantee, its successors or assigns and the said percentage shall be *in lieu of all taxes on this franchise or earnings thereof.* Provided,** That the grantee, its successors or assigns shall continue to be liable for income taxes payable under Title II of the National Internal Revenue Code pursuant to Section 2 of Executive Order No. 72 unless the latter enactment is amended or repealed, in which case the amendment or repeal shall be applicable thereto.

The grantee shall file the return with and pay the tax due thereon to the Commissioner of Internal Revenue or his duly authorized representative in accordance with the National Internal Revenue Code and the return shall be subject to audit by the Bureau of Internal Revenue. [Emphasis supplied.]

The petitioner posits that SMART's claim for exemption under its franchise is not equivocal enough to prevail over the specific grant of power to local government units to exact taxes from businesses operating within its territorial jurisdiction under Section 137 in relation to Section 151 of the LGC. More importantly, it claimed that exemptions from taxation have already been removed by Section 193 of the LGC:

Section 193. *Withdrawal of Tax Exemption Privileges.* -- Unless otherwise provided in this Code, **tax exemptions or incentives granted to, or presently enjoyed by all persons, whether natural or juridical,** including government-owned or controlled corporations, except local water districts, cooperatives duly registered under RA No. 6938, non-stock and non-profit hospitals and educational institutions, **are hereby withdrawn upon the effectivity of this Code.** [Emphasis supplied.]

The petitioner argues, too, that SMART's claim for exemption from taxes under Section 9 of its franchise is not couched in plain and unequivocal language such that it restored the

withdrawal of tax exemptions under Section 193 above. It claims that "if Congress intended that the tax exemption privileges withdrawn by Section 193 of RA 7160 [LGC] were to be restored in respondent's [SMART's] franchise, it would have so expressly provided therein and not merely [restored the exemption] by the simple expedient of including the 'in lieu of all taxes' provision in said franchise."^[10]

We have indeed ruled that by virtue of Section 193 of the LGC, all tax exemption privileges then enjoyed by all persons, save those expressly mentioned, have been withdrawn effective January 1, 1992 - the date of effectivity of the LGC.^[11] The first clause of Section 137 of the LGC states the same rule.^[12] However, the withdrawal of exemptions, whether under Section 193 or 137 of the LGC, pertains only to those already existing when the LGC was enacted. The intention of the legislature was to remove all tax exemptions or incentives granted *prior* to the LGC.^[13] As SMART's franchise was made effective on March 27, 1992 - after the effectivity of the LGC - Section 193 will therefore not apply in this case.

But while Section 193 of the LGC will not affect the claimed tax exemption under SMART's franchise, we fail to find a categorical and encompassing grant of tax exemption to SMART covering exemption from *both* national and local taxes:

R.A. No 7294 does not expressly provide what kind of taxes SMART is exempted from. It is not clear whether the "in lieu of all taxes" provision in the franchise of SMART would include exemption from local or national taxation. **What is clear is that SMART shall pay franchise tax equivalent to three percent (3%) of all gross receipts of the business transacted under its franchise. But whether the franchise tax exemption would include exemption from exactions by both the local and the national government is not unequivocal.**

The uncertainty in the "in lieu of all taxes" clause in R.A. No. 7294 on whether SMART is exempted from both local and national franchise tax must be construed strictly against SMART which claims the exemption.

[Emphasis supplied.]^[14]

Justice Carpio, in his Separate Opinion in *PLDT v. City of Davao*,^[15] explains why:

The proviso in the first paragraph of Section 9 of Smart's franchise states that the grantee shall "continue to be liable for income taxes payable under Title II of the National Internal Revenue Code." Also, the second paragraph of Section 9 speaks of tax returns filed and taxes paid to the "Commissioner of Internal Revenue or his duly authorized representative in accordance with the National Internal Revenue Code." Moreover, the same paragraph declares that the tax returns "shall be subject to audit by the Bureau of Internal Revenue." Nothing is mentioned in Section 9 about local taxes. The clear intent is for the "in lieu of

all taxes" clause to apply only to taxes under the National Internal Revenue Code and not to local taxes.

Nonetheless, even if Section 9 of SMART's franchise can be construed as covering local taxes as well, reliance thereon would now be unavailing. The "in lieu of all taxes" clause basically exempts SMART from paying all other kinds of taxes for as long as it pays the 3% franchise tax; it is the franchise tax that shall be in lieu of all taxes, and not any other form of tax.^[16] Franchise taxes on telecommunications companies, however, have been abolished by R.A. No. 7716 or the Expanded Value-Added Tax Law (*E-VAT Law*), which was enacted by Congress on January 1, 1996.^[17] To replace the franchise tax, the E-VAT Law imposed a 10%^[18] value-added tax on telecommunications companies under Section 108 of the National Internal Revenue Code.^[19] The "in lieu of all taxes" clause in the legislative franchise of SMART has thus become *functus officio*, made inoperative for lack of a franchise tax.^[20]

SMART's claim for exemption from local business and franchise taxes based on Section 9 of its franchise is therefore unfounded.

Claim for Exemption Under Public Telecoms Act

SMART additionally invokes the "equality clause" under Section 23 of the Public Telecoms Act:

SECTION 23. *Equality of Treatment in the Telecommunications Industry.* -- Any advantage, favor, privilege, exemption, or immunity granted under existing franchises, or may hereafter be granted, shall *ipso facto* become part of previously granted telecommunications franchise and shall be accorded immediately and unconditionally to the grantees of such franchises: Provided, however, That the foregoing shall neither apply to nor affect provisions of telecommunications franchises concerning territory covered by the franchise, the life span of the franchise, or the type of service authorized by the franchise. [Emphasis supplied.]

As in the case of *SMART v. City of Davao*,^[21] SMART posits that since the franchise of telecommunications companies granted after the enactment of its franchise contained provisions exempting these companies from both national and local taxes, these privileges should extend to and benefit SMART, applying the "equality clause" above. The petitioner, on the other hand, believes that the claimed exemption under Section 23 of the Public Telecoms Act is similarly unfounded.

We agree with the petitioner.

Whether Section 23 of the cited law extends tax exemptions granted by Congress to new

franchise holders to existing ones has been answered in the negative in the case of *PLDT v. City of Davao*.^[22] The term "exemption" in Section 23 of the Public Telecoms Act does not mean tax exemption; rather, it refers to exemption from certain regulatory or reporting requirements imposed by government agencies such as the National Telecommunications Commission. The thrust of the Public Telecoms Act is to promote the gradual deregulation of entry, pricing, and operations of all public telecommunications entities, and thus to level the playing field in the telecommunications industry. The language of Section 23 and the proceedings of both Houses of Congress are bereft of anything that would signify the grant of tax exemptions to all telecommunications entities.^[23] Intent to grant tax exemption cannot therefore be discerned from the law; the term "exemption" is too general to include tax exemption and runs counter to the requirement that the grant of tax exemption should be stated in clear and unequivocal language too plain to be beyond doubt or mistake.

Surcharge and Interests

Since SMART cannot validly claim any tax exemption based either on Section 9 of its franchise or Section 23 of the Public Telecoms Act, it follows that petitioner can impose and collect the local franchise and business taxes amounting to P764,545.29 it assessed against SMART. Aside from these, SMART should also be made to pay surcharge and interests on the taxes due.

The settled rule is that good faith and honest belief that one is not subject to tax on the basis of previous interpretation of government agencies tasked to implement the tax laws are sufficient justification to delete the imposition of surcharges and interest.^[24] In refuting liability for the local franchise and business taxes, we do not believe SMART relied in good faith in the findings and conclusion of the Bureau of Local Government and Finance (*BLGF*).

In a letter dated August 13, 1998, the *BLGF* opined that SMART should be considered exempt from the franchise tax that the local government may impose under Section 137 of the *LGC*.^[25] SMART, relying on the letter-opinion of the *BLGF*, invoked the same in the administrative protest it filed against petitioner on February 15, 2002, as well as in the petition for prohibition that it filed before the *RTC* of Iloilo on April 30, 2002. However, in the 2001 case of *PLDT v. City of Davao*,^[26] we declared that we do not find *BLGF*'s interpretation of local tax laws to be authoritative and persuasive. The *BLGF*'s function is merely to provide consultative services and technical assistance to the local governments and the general public on local taxation, real property assessment, and other related matters.^[27] Unlike the Commissioner of Internal Revenue who has been given the express power to interpret the Tax Code and other national tax laws,^[28] no such power is given to the *BLGF*. SMART's dependence on *BLGF*'s interpretation was thus misplaced.

WHEREFORE, we hereby **GRANT** the petition and **REVERSE** the decision of the *RTC* dated January 19, 2005 in Civil Case No. 02-27144 and find SMART liable to pay the local

franchise and business taxes amounting to P764,545.29, assessed against it by petitioner, plus the surcharges and interest due thereon.

SO ORDERED.

Quisumbing, (Chairperson), Carpio Morales, Velasco, Jr., and Nachura, JJ., concur.*

* Designated additional member of the Second Division per Special Order No. 571 dated February 12, 2009.

[1] Civil Case No. 02-27144.

[2] Decision dated January 19, 2005, penned by Judge Loida J. Diestro-Maputol; *rollo*, pp. 35-39.

[3] *Id.*, p. 37.

[4] G.R. No. 155491, September 16, 2008.

[5] 35 Phil. 42 (1916).

[6] 49 Phil. 466 (1926).

[7] G.R. No. L-12134, November 30, 1961, 3 SCRA 591, citing *House v. Posadas*, 53 Phil. 338 (1929) and *CIR v. Manila Jockey Club, Inc.*, 98 Phil. 670 (1956).

[8] G.R. No. L-23041, July 31, 1969, 28 SCRA 1119, citing *Memphis v. U & P Bank*, 91 Tenn. 546, 550, and *Farrington v. Tennessee and County of Shelby*, 95 U.S. 679, 686.

[9] G.R. No. 156040, December 11, 2008.

[10] *Rollo*, p. 20.

[11] *Philippine Long Distance Telephone Company, Inc. (PLDT) v. City of Bacolod, et al.*, G.R. No. 149179, July 15, 2005, 463 SCRA 528; *Mactan Cebu International Airport Authority v. Marcos*, G.R. No. 120082, September 11, 1986, 261 SCRA 667.

[12] Section 137. *Franchise Tax.* - **Notwithstanding any exemption granted by any law or other special law**, the province may impose a tax on businesses enjoying a franchise, at

the rate not exceeding fifty percent (50%) of one percent (1%) of the gross annual receipts for the preceding calendar year based on the incoming receipt, or realized within its territorial jurisdiction. x x x. [Emphasis supplied.]

[13] *SMART v. City of Davao*, *supra* note 4.

[14] *Id.*

[15] G.R. No. 143867, March 25, 2003, 399 SCRA 442.

[16] *Id.*

[17] Amended by R.A. No. 9337 or the Revised Value-Added Tax Law (*R-VAT Law*).

[18] The tax rate is now 12% per R-VAT Law.

[19] *Radio Communications of the Philippines, Inc. (RCPI) v. Provincial Assessor of South Cotabato, et al.*, G.R. No. 144486, April 13, 2005, 456 SCRA 1.

[20] *Digital Telecommunications Philippines, Inc. v. Province of Pangasinan*, G.R. No. 152534, February 23, 2007, 516 SCRA 541.

[21] *Supra* note 15.

[22] G.R. No. 143867, August 22, 2001, 363 SCRA 522; see also note 15.

[23] *SMART v. City of Davao*, *supra* note 4.

[24] *Michel J. Lhuillier Pawnshop, Inc. v. Commissioner of Internal Revenue*, G.R. No. 166786, September 11, 2006, 501 SCRA 450, citing *Connell Bros. Co. (Phil.) v. Collector of Internal Revenue*, 119 Phil. 40 (1963).

[25] *Rollo*, p. 48.

[26] *Supra* note 22; see also note 15.

[27] ADMINISTRATIVE CODE, Title II, Chapter 4, Section 33 (4)

[28] SEC. 4. *Power of the Commissioner to Interpret Tax Laws and to Decide Cases.* - The power to interpret the provisions of this Code [NIRC] and other tax laws shall be under the exclusive and original jurisdictions of the Commissioner, subject to review by the

