REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

PHILIPPINE LONG DISTANCE TELEPHONE COMPANY,
Petitioner,

- versus - C.T.A. CASE NO. 4056

COMMISSIONER OF INTERNAL REVENUE,
Respondent.
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D E C I S I O N

Disputed by petitioner Philippine Long Distance Telephone Company is the correctness and validity of the deficiency income tax liability in the amount of P495,425,391.00 for the taxable years 1969 to 1980 assessed against it by respondent Commissioner of Internal Revenue.

The uncontroverted facts as set forth in respondent's memorandum are as follows:

> Petitioner Philippine Long Distance Telephone Company (PLDT for short), a corporation duly organized and existing under the laws of the Republic of the

Philippines, was enfranchised to render local and international telephone service on November 28, 1928 under Public Act No. 3436, as amended by Commonwealth Act No. 407, for a period of 50 years or until November 28, 1978. Under Section 7 of said Public Act No. 3436, it was provided that the payment of 1% franchise tax on all gross receipts of the telephone and other electrical transmission business transacted under the franchise shall be "in lieu of all taxes" on the franchise or earnings thereof.

On November 9, 1970, Republic Act No. 6146 was passed extending the life of PLDT's franchise granted under Public Act No. 3436 to another twenty-five years from the date of its expiration on November 28, 1978, "under the terms and conditions therein provided" and "that during the twenty-five-year period herein granted as extension, the grantee, its successors or assigns shall pay its franchise tax at an increased rate of five per centum". (Section 1, R.A. No. 6146)

On June 11, 1978, Presidential Decree No. 1528 was promulgated requiring PLDT to pay a franchise tax of 2% thereby modifying the rate of 5% provided for in Republic Act No. 6146, effective immediately up to the end of the twenty-five year extended period. Said P.D. 1528 also provides that "except for the change in the rate of franchise tax herein prescribed, it shall be subject to the same terms and conditions as already provided for under existing laws."

On March 30, 1984, upon investigation conducted by respondent's examiners, PLDT was assessed in the total amount of P980,371,787.37 as deficiency income and withholding taxes for the years 1969 to 1980, inclusive of interests and penalties (Exhibit 1, p. 73, BIR Rec.), which assessment was assailed in PLDT's letter dated May 25, 1984 (Exhibit B, Petitioner).

On March 20, 1986, respondent issued his decision on PLDT's protest reducing the tax assessment to P787,234,718.46 (Exhibit 2, pp. 297-304, BIR Rec.).

From the above decision, petitioner appealed to this Court. However, as a result of the modification made by respondent in the administrative reinvestigation conducted after the filing of the petition for review, as well as the availment by petitioner of the provisions of Executive Order No. 44, the assessed amount of P787,234,718.46 was further reduced to P495,425,391.00 representing the total of the basic deficiency income taxes on petitioner's franchise operations for the taxable years 1969 to 1980.

The remaining issues now limited to the validity of the deficiency income tax liability of petitioner in the amount of P495,425,391.00 are:

1. Whether or not petitioner's income tax exemption repealed pursuant to Section 24(d) [now 24(c)] as inserted by Republic Act No. 5431 was

restored by Republic Act No. 6146 which took effect on November 9, 1970.

2. Whether or not the issuance of the 1969 to 1980 deficiency income tax assessment against taxpayer on March 30, 1984 was in contravention of the provision of Section 338-A (now Section 278) of the National Internal Revenue Code on non-retroactivity of rulings.

On the first issue, respondent contends that the income tax exemption of petitioner as provided for in its charter that the payment of the franchise tax therein shall be in lieu of any and all taxes, has been repealed by Section 24(d) [now Section 24(c)] of the National Internal Revenue Code inserted by Republic Act No. 5431 promulgated on June 27, 1968 and therefore petitioner has become liable for the payment of income tax starting from its taxable year 1969.

Section 24(d) reads as follows:

> (d) The provisions of existing special or general laws to the contrary notwithstanding all corporate taxpayers not specifically exempt under Section 27 of this Code shall pay the rates provided in this section. All corporations, agencies, or instrumentalities owned or controlled by the Government, including

> the Government Service Insurance System and the Social Security System but excluding educational institutions, shall pay such rate of tax upon their taxable net income as are imposed by this section upon associations or corporations engaged in a similar business or industry.

As interpreted by the Court of Tax Appeals in **Koronadal Electric Light & Power Co., Inc. vs. Commissioner of Internal Revenue**, CTA Case No. 2600, June 26, 1979 (not appealed); the Supreme Court in **Radio Communications of the Philippines vs. Court of Tax Appeals, et al.**, G.R. No. 60547, Resolution En Banc dated July 11, 1985 and **Cagayan Electric Power & Light Co., Inc. vs. Commissioner of Internal Revenue, et al.**, G.R. No. 60126, September 25, 1985, 138 SCRA 629, the income tax exemption of corporate franchise holders has been withdrawn by Republic Act No. 5431. Thus, in the later case of **Cagayan Electric Power & Light Co., Inc.**, the Supreme Court held:

> xxx xxx xxx
>
> On June 27, 1968, Republic Act No. 5431 amended section 24 of the Tax Code by making liable for income tax <u>all corporate taxpayers</u> not specifically exempt under paragraph (c)(1) of said section and section 27 of the Tax Code notwithstanding the "provisions of

> existing special or general laws to the contrary". Thus, franchise companies were subjected to <u>income tax in addition to franchise tax</u>.
>
> Republic Act No. 5431, in amending section 24 of the Tax Code by subjecting to income tax all corporate taxpayers not expressly exempted therein and in section 27 of the Code, had the effect of <u>withdrawing petitioner's exemption from income tax</u>.
>
> xxx xxx xxx

Petitioner does not question the legality of the rulings laid down in the aforecited cases insofar as it affects franchises granted prior to the effective date of Republic Act No. 5431 but asserts that the subsequent enactment of Republic Act No. 6146 on November 9, 1970 amending petitioner's original franchise, has restored petitioner's exemption from income tax, thus its liability for income tax would only be for the period January 1, 1969 to November 9, 1970. (Exh. F-1, pp. 477-478, BIR records; p. 169, CTA records.)

The provisions of Republic Act No. 6146 amending petitioner's franchise, reproduced in full are as follows:

[REPUBLIC ACT No. 6146]

"AN ACT EXTENDING THE TERM OF THE FRANCHISE GRANTED TO THE PHILIPPINE LONG DISTANCE TELEPHONE COMPANY UNDER ACT NUMBERED THREE THOUSAND FOUR HUNDRED AND THIRTY-SIX, AS AMENDED BY COMMONWEALTH ACT NUMBERED FOUR HUNDRED AND SEVEN, AND FOR OTHER PURPOSES.

"Be it enacted by the Senate and House of Representatives of the Philippines in Congress assembled:

"SECTION 1. The term of the franchise granted to the Philippine Long Distance Telephone Company under Act Number Three thousand four hundred and thirty-six, as amended by Commonwealth Act Numbered Four hundred and seven, is hereby extended, under the terms and conditions therein provided, for a period of twenty-five years from the date of its expiration: Provided, That during the twenty-five-year period herein granted as extension, the grantee, its successors or assigns shall pay its franchise tax at an increased rate of five per centum.

SECTION 2. This Act shall take effect upon its approval.

"Approved, November 9, 1970."

Petitioner submits that Republic Act No. 6146 is a "reference statute" that extended the term of its original franchise under Public Act No. 3436 as amended by Commonwealth Act No. 407 for a period of twenty-five years at an increased rate of franchise tax amounting to five per centum "under the terms and conditions therein provided." It is urged that the specific adoption by reference of the terms and conditions contained in the earlier acts serves to lift such terms and conditions from the adopted statute and bodily incorporates them in the adopting statute as if it had been written at full length, without the necessity of a verbatim repetition thereof in the adopting statute. From the bare wordings of Republic Act No. 6146, the legislative intention was only to revive or re-enact all the "terms and conditions" provided in petitioner's original franchise, including the "in lieu of all taxes" provisions contained in Section 7 therein, which was withdrawn by Republic Act No. 5431. Any effect of Republic Act No. 5431 withdrawing the income tax exemption granted under petitioner's original franchise has been negated and neutralized by the passage of Republic Act No. 6146 specifically adopting by reference and re-enacting the "in lieu of all taxes" provision contained in Section 7 of petitioner's original charter, effective November 9, 1970. (Petitioner's memorandum, pp. 172-173, CTA records.)

We are unable to agree with petitioner.

It is not disputed that Republic Act No. 6146 is a reference statute or a statute of specific reference. As aptly quoted by respondent, "a statute of specific reference incorporates the provisions referred to from the statute as of the time of adoption without subsequent amendments unless the legislature has expressly or by strong implication shown its intention to incorporate subsequent amendments with the statute". (Sutherland Statutory Construction, Vol. 2, p. 548, or Vol. 2A, p. 324, underscoring supplied.) The above-mentioned "subsequent amendments" refer to amendments to the adopted statute after the time of its adoption and not prior to the time of its adoption by the reference statute. Since Republic Act No. 5431 enacted on June 27, 1968 had already amended petitioner's original franchise by withdrawing its exemption from income tax prior to its adoption by the reference statute, Republic Act No. 6146, on November 9, 1970, obviously, the terms and conditions incorporated in Republic Act No.

6146 no longer included such exemption from income tax.

Presidential Decree No. 1528, issued on June 11, 1978, a subsequent amendment to petitioner's franchise modifying the rate of petitioner's franchise tax to 2%, also adopted the terms and conditions of petitioner's existing franchise minus its exemption from income tax which had already been withdrawn by Republic Act No. 5431. The pertinent provision of Presidential Decree No. 1528 reads as follows:

> "SECTION 1. The provisions of existing law to the contrary notwithstanding, the Philippine Long Distance Telephone Company, its successors and assigns, shall pay a franchise tax at the rate of two per centum of all gross receipts of the telephone or other electrical transmission business transacted under its franchise, effective immediately upon the issuance of this Decree and up to the end of the twenty-five years extended term of its franchise under Republic Act No. 6146; Provided, That, except for the change in the rate of franchise tax herein prescribed, it shall be subject to the same terms and conditions as already provided for under existing laws." (Underscoring supplied.)

The insertion in the above provision of the phrase "as already provided for under existing laws" is an indication of the intention to have existing enactments touching the referred statute, construed and applied in harmony with it. These would include the repeal of petitioner's income tax exemption by Republic Act No. 5431. In terms of legislative intent, it is assumed that whenever the legislature enacts a provision it has in mind previous statutes relating to the same subject matter, wherefore it is held that in the absence of any express repeal or amendment therein, the new provision was enacted in accord with the legislative policy embodied in these prior statutes, and they all should be construed together. (Sutherland, Statutory Construction, Vol. 2A, p. 290.)

In support of its stand that the passage of Republic Act No. 6146 has re-enacted the "in lieu of all taxes" provision in its original charter, petitioner cites the case of Cagayan Electric Power & Light Co., Inc. vs. Commissioner of Internal Revenue, et al., supra, where the Supreme Court ruled that the withdrawal of the income tax exemption in the original charter of franchisee therein by virtue of Republic Act No. 5431, was restored by the subsequent legislation which re-enacted the income tax exemption in its franchise.

The above-cited case is not decisive insofar as the full restoration of petitioner's income tax exemption is concerned. As adverted to earlier, it is applicable to the instant case only to the extent relied on by respondent, that Republic Act No. 5431 had repealed the income tax exemption of petitioner. In fact, in passing, the Supreme Court commented in its decision there that:

> "It is relevant to note that franchise companies like the Philippine Long Distance Telephone Company, have been paying income tax, in addition to the franchise tax."

In that case, the income tax exemption of petitioner therein, the Cagayan Electric Power & Light Co., Inc., was restored by the express re-enactment of its income tax exemption in Section 3 of Republic Act No. 6020 promulgated on August 4, 1969, as follows:

> "SEC. 3. In consideration of the franchise and rights hereby granted, the grantee shall pay a franchise tax equal to three *per centum* of the gross earnings for electric current sold under this franchise, of which two *per centum* goes

> into the National Treasury and one *per centum* goes into the treasury of the Municipalities of Tagoloan, Opol, Villanueva and Jasaan and Cagayan de Oro City, as the case may be: *Provided*, That the said franchise tax of three *per centum* of the gross earnings shall be in lieu of all taxes and assessments of whatever authority upon privileges, earnings, income, franchise, and poles, wires, transformers, and insulators of the grantee from which taxes and assessments the grantee is hereby expressly exempted." (Underscoring supplied.)

In the present case there was no such express re-enactment in Republic Act No. 6146 nor in Presidential Decree No. 1528, the amendments to petitioner's original franchise, of the "in lieu of all taxes" provision of Section 7 of Public Act No. 3436, petitioner's original charter. The principle that tax exemption laws are strictly construed against the exemption is specially applicable to contracts granting exemption from taxation. Such contracts are in derogation of the sovereign authority and of common right, and therefore are not to be extended beyond the exact and express requirements of the language used, construed *strictissimi juris*. An exemption from taxation, in order to constitute a contract binding on the state, must be clearly and unequivocally expressed. Every reasonable doubt should be resolved against an exemption and in favor of the taxing power of the state. The intention to grant such immunity must be clear beyond a reasonable doubt and the language used must admit of no other reasonable construction. (51 Am Jur., pp. 515-516.)

The rule is well settled that one who claims to be exempt from the payment of a particular tax must do so under clear and unmistakable terms found in the statute. Tax exemptions are strictly construed against the taxpayer; they being highly disfavored and may almost be said "to be odious to the law." He who claims an exemption must be able to point to some positive provision of law creating the right; it cannot be allowed to exist upon a mere vague implication or inference. (**Asiatic Petroleum vs. Llanes**, 49 Phil. 466, 471; **Union Garment Co., Inc. vs. Court of Tax Appeals**, L-16809, January 31, 1962, 4 SCRA 304; **Philippine Acetylene Co., Inc. vs. Commissioner of Internal Revenue**, L-190707, August 17, 1967, 20 SCRA 1056; **Republic Flour Mills, Inc. vs. Commissioner of**

Internal Revenue, L-25602, February 18, 1970, 31 SCRA 520; **Commissioner of Customs vs. Philippine Acetylene Co. & Court of Tax Appeals**, L-22443, May 29, 1971, 39 SCRA 71; **Davao Light and Power Co., Inc. vs. Commissioner of Customs**, L-28902, March 29, 1972, 44 SCRA 122.) The right of taxation will not be held to have been surrendered unless the intention to surrender is manifested by words too plain to be mistaken (**Ohio Life Insurance & Trust Co. vs. Debolt**, 60 Howard, 416), for the state cannot strip itself of the most essential power of taxation by doubtful words; it cannot, by ambiguous language, be deprived of this highest attribute of sovereignty (**Erie Railway Co. vs. Commonwealth of Pennsylvania**, 21 Wallace, 492, 499). So, when exemption is claimed, it must be shown indubitably to exist, for every presumption is against it, and a well-founded doubt is fatal to the claim (**Farrington vs. Tennessee & County of Shelby**, 95 U.S. 679,686). (**Asiatic Petroleum Co. vs. Llanes**, 49 Phil. 466, 471; **Manila Electric Company vs. Commissioner of Internal Revenue**, L-29987 & L-23844, October 22, 1975, 67 SCRA 351.)

Clearly, the income tax exemption of petitioner withdrawn by Republic Act No. 5431 was not restored by Republic Act No. 6146 nor by Presidential Decree No. 1528.

We now consider the second issue: Petitioner's alternative argument that the issuance of the 1969 to 1980 deficiency income tax assessment against petitioner was in contravention of the provision of Section 338-A (now Section 278) of the National Internal Revenue Code on non-retroactivity of rulings.

The record shows that in a letter dated May 14, 1969, petitioner's counsel, on behalf of its client Clavecilla Radio System, Inc. requested from the then Commissioner of Internal Revenue, reconsideration of the ruling in Revenue Memorandum Circular No. 41-68 dated November 15, 1968 holding that "all corporations enjoying exemption from income tax by virtue of their franchises are now subject to income tax in view of the amendment of Section 24 of the Tax Code by Republic Act No. 5431."

In a letter dated June 16, 1969, the Commissioner granted the above request for reconsideration as follows: (Exh. "G")

June 16, 1969

Messrs. Meer, Meer and Meer
Attorneys-at-Law
9th Floor
PLDT Building
Legaspi Street
Makati, Rizal

Gentlemen:

This refers to your letter dated May 14, 1969, requesting on behalf of your client, the Clavecilla Radio System, Inc., reconsideration of that ruling in Revenue Memorandum Circular No. 41-68, dated November 15, 1968, holding that all corporations enjoying exemption from income tax by virtue of their franchises are now subject to income tax in view of the amendment of Section 24 of the Tax Code by Republic Act No. 5431.

In reply, I have the honor to inform you that after a thorough and analytical study of the amendatory provision in question, and considering that franchises are of the nature of contracts between the government and the grantees thereof, this Office has arrived at the conclusion that the said amendatory provision could not have contemplated the withdrawal of the tax exemption of franchise grantees for such withdrawal would impair the obligation of contracts between the government and the grantee, which is prohibited by the constitution.

In view of the foregoing, and considering that the Secretary of Justice in interpreting a similar provision of

> law ruled that said law did not apply to the Manila Railroad Company, a franchise grantee, (Opinion No. 227, series of 1948) it is the opinion of this Office that Republic Act No. 5431 did not repeal the exemption granted in the franchise of your client. Accordingly, your client and other franchise grantees similarly situated shall be subject to tax conformably with the provisions of their respective franchises.
>
> Very truly yours,
>
> MISAEL P. VERA
> Commissioner of Internal Revenue

To confirm the applicability of the Clavecilla ruling to its client, petitioner herein, petitioner's counsel requested for a direct ruling for the Philippine Long Distance Telephone Company.

The pertinent excerpts of the confirmatory ruling issued by the Commissioner of Internal Revenue on July 3, 1969 read: (Exh. "G-1")

> This refers to your letter dated July 2, 1969 requesting confirmation on behalf of your client, the Philippine Long Distance Telephone Company (PLDT), that the ruling contained in our letter dated June 16, 1969, to the effect that Republic Act No. 5431 did not repeal the exemption from income tax granted in the franchise of the Clavecilla Radio System, Inc. and that the Clavecilla Radio System, Inc. and other franchise grantees similarly situated are subject to tax conformably with the provisions of their respective franchises, is applicable to your client.

> On the basis of Sec. 7 of your franchise, as quoted in your letter, which is similar to the tax provision in the Clavecilla franchise, our ruling in the Clavecilla query is applicable to the Philippine Long Distance Telephone Company.

Petitioner contends that from the time the ruling of July 3, 1969 was issued by the Commissioner specifically exempting petitioner from the payment of income tax under its franchise, respondent has not issued for an uninterrupted period of fourteen years, any notification or ruling addressed to petitioner revoking, modifying or reversing said ruling or the Clavecilla ruling, until March 30, 1984 when respondent assessed petitioner for income taxes for the years 1969 to 1980. In violation of Section 338-A (now Section 278) of the National Internal Revenue Code respondent, in effect, reversed his rulings retroactively to the prejudice of petitioner who, relying on these rulings, was precluded from including said income tax liability in its rate base and deprived of the right to apply for an increase in subscriber's rates commensurate to such an expense to enable petitioner to receive the fair return of 12% allowed to public utilities.

Section 338-A (now Section 278) of the National Internal Revenue Code reads:

> SEC. 338-A. Non-retroactivity of rulings. Any revocation, modification, or reversal of any of the rules and regulations promulgated in accordance with the preceding section or any of the rulings or circulars promulgated by the Commissioner of Internal Revenue shall not be given retroactive application if the revocation, modification, or reversal will be prejudicial to the taxpayer except in the following cases: (a) where the taxpayer deliberately misstates or omits material facts from his return or in any document required of him by the Bureau of Internal Revenue; (b) where the facts subsequently gathered by the Bureau of Internal Revenue are materially different from the facts on which the ruling is based; or (c) where the taxpayer acted in bad faith.

For his part, respondent avers that the aforementioned rulings dated June 16 and July 3, 1969 issued by the then Commissioner of Internal Revenue are null and void, having been shown to be contrary to the provisions of the National Internal Revenue Code. There being no ruling to speak of, no vested right accrued under these rulings, thus any revocation or modification thereof may be given retroactive effect without contravening the provision of Section 338-A (now Section 278) of the National Internal Revenue Code in line with the doctrine laid down in the case of **Hilado vs. Collector of Internal Revenue**, 100 Phil. 288. It is contended further that the decision to assess and collect from petitioner deficiency income taxes retroactively for the years 1969 to 1980 is in accordance with the Resolution En Banc rendered by the Supreme Court in the case of **Radio Communications of the Philippines, Inc. (RCPI for short) vs. Court of Tax Appeals, et al.**, G.R. No. 60547, July 11, 1985.

Petitioner maintains that the authorities relied on by respondent in support of the principle that the government is not barred from effecting collection of the proper taxes due and collectible from taxpayers, were decided by the courts on issues of fact and law obtaining prior to the enactment of Section 338-A of the National Internal Revenue Code on August 9, 1969 and are therefore immaterial and irrelevant to the determination of the effect of said Section 338-A to this case. And the efficacy of the doctrine in the Hilado case has already been negated by the dicta of the Supreme Court in the cases of **ABS-CBN Broadcasting**

Corporation vs. Court of Tax Appeals and the Commissioner of Internal Revenue, L-52306, October 12, 1981, 108 SCRA 142, and the **Commissioner of Internal Revenue vs. Burroughs, Ltd. and the Court of Tax Appeals**, L-66653, June 19, 1986, 142 SCRA 324 which are now controlling.

The position taken by petitioner, to our mind, is meritorious. The doctrine that the government is never estopped from collecting a tax that is legally due it, now stands qualified by Section 338-A (now Section 278) of the National Internal Revenue Code, in the sense that under that section, rulings and circulars, rules and regulations, promulgated by the Commissioner of Internal Revenue would have no retroactive application if to so apply them would be prejudicial to taxpayers, except in the three instances enumerated therein.

The ABS-CBN case and the Burroughs case above-cited by petitioner are in point. In both cases, the Supreme Court applied Section 338-A, having found that the prejudice to petitioner therein of the retroactive application of the revocation of the rulings involved "is beyond question" and "in so far as the enumerated exceptions are concerned, admittedly, petitioner does not fall under any of them." Thus, in the ABS-CBN case, the Supreme Court observed, in closing:

> This Court is not unaware of the well entrenched principle that the Government is never estopped from collecting taxes because of mistakes or errors on the part of its agents. In fact, utmost caution should be taken in this regard. But, like other principles of law, this also admits of exceptions in the interest of justice and fair play. The insertion of Section 338-A into the National Internal Revenue Code, as held in the case of Tuason, Jr. vs. Lingad, is indicative of legislative intention to support the principle of good faith. In fact, in the United States, from where Sec. 24(b) was patterned, it has been held that the Commissioner or Collector is precluded from adopting a position inconsistent with one previously taken where injustice would result therefrom, or where there has been a misrepresentation to the taxpayer.

The RCPI case cited by respondent is not controlling. In the resolution of the Supreme Court dated July 11, 1985, the only issue raised and resolved by the Court was the effect of Section 24 of Republic Act No. 5431 on the tax exemption of the franchise of petitioner therein and did not involve the proper interpretation of Section 338-A (now Section 278) of the National Internal Revenue

Code which is the issue presently under consideration. This is evident from the ruling of the Supreme Court as follows:

> x x x x The issue raised to this Court now is the validity of the respondent court's decision which ruled that the exemption under Republic Act No. 4054 was repealed by Section 24 of Republic Act No. 5431, dated June 27, 1968 which reads:
>
> > (d) The provisions of existing special or general laws to the contrary notwithstanding, all corporate taxpayers not specifically exempt under Sections 24(c)(1) and 27 of this Code shall pay the rates provided in this section. All corporations, agencies, or instrumentalities owned or controlled by the government, including the Government Service Insurance System and the Social Security System but excluding educational institutions, shall pay such rate of tax upon their taxable net income as are imposed by this section upon associations or corporations engaged in a similar business or industry." (Underlining supplied.)
>
> > An examination of Section 24 of the Tax Code as amended shows clearly that the law intended all corporate taxpayers to pay income tax as provided by the statute. There can be no doubt as to the power of Congress to repeal the earlier exemption it granted.

> Article XIV, Section 8 of the 1935 Constitution and Article XIV, Section 5 of the Constitution as amended in 1973 expressly provide that no franchise shall be granted to any individual, firm, or corporation except under the condition that it shall be subject to amendment, alteration, or repeal by the legislature when the public interest so requires. There is no question as to the public interest involved. The country needs increased revenues. The repealing clause is clear and unambiguous. There is a listing of entities entitled to tax exemption. The petitioner is not covered by the provision. Considering the foregoing, the Court resolved to DENY the petition for lack of merit. The decision of the respondent court is affirmed.

Here in the case at bar, which is on all fours with the ABS-CBN case, supra, the prejudice to petitioner of the retroactive application of respondent's deficiency income tax assessment, which in effect revoked the ruling issued to petitioner on July 3, 1969, has been sufficiently established. And there is no showing that petitioner falls under any of the three exceptions specified in Section 338-A.

The records show that from July 3, 1969, when the Commissioner of Internal Revenue issued the ruling exempting petitioner from the payment of income tax under its franchise, respondent has not issued any notification or ruling addressed to petitioner revoking, modifying or reversing said ruling until by his assessment dated March 30, 1988, respondent assessed petitioner for deficiency income taxes for the years 1969 to 1980. (t.s.n., pp. 14-18, April, 1987.)

Petitioner's lone witness, its Senior Executive Vice-President and General Counsel, testified that relying on the assurance of the Commissioner of Internal Revenue that petitioner was exempt from income tax, inspite of the enactment of Republic Act No. 5431, petitioner did not include said taxes as an element of cost in applying for the approval by the regulatory body of the rates payable by its subscribers. Thus, petitioner would be prejudiced irreparably by its payment of the P495,425,391.00 assessment as it would be impossible to retroactively readjust its rates from 1969 to 1980 and shift such cost to its subscribers during that period. His explanation for this is as follows: (t.s.n., pp. 24-25, April 1, 1987.)

CROSS EXAMINATION
ATTY. PANGILINAN

Q. If your company is finally adjudged liable for the deficiency income taxes for the years 1969 to 1980 in 1987 or at any later date, is it not possible for PLDT to recoup such expense for the prior period by applying to the National Telecommunications for an increase in rate in order to cover such cost?

A. That is not possible. In the first place, a rate order or judgment only operates prospectively, never retroactively. The rate adjustment will only be based on the current expenses or cost and such other factors in order to provide a public utility rate that is fair and reasonable on a prospective basis. Elements of cost or expenses, such as taxes for past periods notably extending back to 1969 cannot be considered in any application for rate adjustment in 1987. Besides, the taxes for the said period should affect the subscribers of PLDT during said period and there is no way we can ask them for an adjustment of the rates that they had previously considered and was not made part of the expenses

> or cost for purposes of fixing the public utility rate then in force.

That taxes are includible as elements of cost in the determination of the cost of service of public utility rate making, is supported by the following authority quoted by petitioner:

> "Where public utilities are concerned, whether public or publicly owned, the tax burden is shifted to consumers through the rate charged for service. Accordingly, taxes are treated as revenue deductions in determining: (a) the actual return which the utility is earning at any particular time; and (b) the rate of return that would result from a specified level of revenues. In determining the cost of service of public utility rate making, it is proper to include as costs the taxes that would be paid if a fair return were earned." (Paul J. Garfield and Wallace F. Lovejoy, Public Utility Economics, Prentice-Hall, Inc., p. 392.)

Undoubtedly, petitioner could have shifted the income tax burden to its subscribers during the years in question if it had not relied on the rulings (Exhs. "G" & "G-1") issued by the Commissioner of Internal Revenue. It is clear from the foregoing that to impose the deficiency income tax assessment on petitioner would be prejudicial to it for petitioner can no longer recover such costs from its subscribers to enable it to earn the 12% rate of return consistently adopted in Philippine decisions as the fair rate of return allowed on the investments of public utilities. (**Manila Electric Company vs. Public Service Commission**, 18 SCRA 651; **Republic of the Philippines vs. Public Service Commission and Manila Electric Company**, 41 SCRA 644.)

At any rate, the prejudice that would result to petitioner Philippine Long Distance Telephone Company by a retroactive application of respondent's deficiency income tax assessment which revoked his rulings of June 16 and July 3, 1969 is beyond question for it will be deprived of the very substantial amount of P495,425,391.00. And insofar as the enumerated exceptions are concerned, admittedly, petitioner does not fall under any of them. (See **Commissioner of Internal Revenue vs. Burroughs Limited**, supra.)

Respondent advances the argument that when the Commissioner of Internal Revenue, under Revenue Memorandum Order No. 15-72 issued on May 17, 1972, reverted to his position that all franchise holders are subject to income tax in view of the amendment of Section 24 of the Tax Code by Republic Act No. 5431, and proceeded to investigate and assess franchise holders for income tax liabilities, why did petitioner not contest such Revenue Memorandum Order to protect its interest?

Petitioner, on the other hand, disowns any knowledge or notice of Revenue Memorandum Order No. 15-72 until July 29, 1986 when respondent served upon petitioner his revised assessment dated July 17, 1986 (Exh. "E") wherein petitioner was advised about such Order for the first time. It is insisted that in the absence of due notice, respondent cannot claim that the rulings contained in Exhibits "G" and "G-1", have already been effectively revoked by the mere issuance of Revenue Memorandum Order No. 15-72.

We find petitioner's contention tenable.

Revenue Memorandum Order No. 15-72 is reproduced hereunder: (Exh. "4")

May 17, 1972

REVENUE MEMORANDUM ORDER NO. 15-72

SUBJECT: Liability of Franchise Holders to Income Tax under Section

<u>24(d) of the Tax Code, as inserted by Republic Act No. 5431.</u>

TO : The Assessment Department, particularly the Income Tax Division, Assessment Branches Investigating Units, particularly the Services & Miscellaneous (Audit) Division and others concerned:

Section 24(d) of the Tax Code, as inserted by Republic Act No. 5431, provides:

> "(d) <u>The provisions of existing special or general laws to the contrary notwithstanding</u>, all corporate taxpayers not specifically exempt under Sections 24(c)(1) and 27 of this Code (referring to the National Internal Revenue Code) shall pay the rates provided in this section. All corporations, agencies, or instrumentalities owned or controlled by the Government, including the Government Service & Insurance System, Social Security System but excluding educational institutions, shall pay such rate of tax upon their taxable net income as are imposed by this section upon associations or corporations engaged in a similar business or industry." (Underscoring supplied)

Pursuant to the abovequoted provision of law, all corporations, except those specifically exempt under Section 24(c)(1) and 27 of the Tax Code, are subject to income tax prescribed in Section 24 of the Tax Code. Accordingly even franchise holders whose franchises contain a provision that the franchise tax prescribed therein shall be in lieu of all taxes are subject to income tax for taxable years beginning after June 30, 1968 (see Section 10, Republic Act No. 5431). This stand is supported by the opinion of the Secretary of Justice, contained in his 3rd Indorsement to the Secretary of Finance, dated March 28, 1969, the pertinent portion of which is quoted hereunder:

> "The contention that Republic Act No. 5431 merely intended to change the existing rates of corporate tax applicable to corporations already subject to income tax and not to lift the tax exemptions granted by special law, is without merit, just as the argument that the term 'corporate taxpayer' should be construed as referring only to those corporations already subject to tax at the time of the amendment. For in providing for the general application of the new tax rates and expressly excluding therefrom 'all corporate taxpayers not specifically exempt under Section . . . 27 of this Code' which significantly refer to entities wholly exempt from income tax, Section 24(d) was evidently meant to be applicable even to corporations enjoying income tax exemption before the enactment of RA 5431. Otherwise, there would have been no need for said exclusion. The resulting conclusions is that outside of those referred to in Section

> 24(c)(1) and 27 of the Tax Code, all corporations whose liability for income tax was before governed by general laws or special statutes applicable to designated classes or groups of corporate entities, are now subject to the rates prescribed in RA 5431."

In view thereof, all investigating and assessment units concerned are hereby instructed to ascertain the income taxes due from franchise holders for the years 1968, 1969, 1970 and 1971 and to issue the corresponding assessments against them.

All internal revenue officers and others concerned are enjoined to give this circular as wide a publicity as possible.

In the Statement of Procedural Rules, par. 601.201(1) in force in U.S. law from where Section 338-A (now Section 278) of our National Internal Revenue Code is patterned, the applicable portions on the "effect of rulings" is quoted below:

"(4) A ruling found to be in error or not in accord with the current views of the Service may be modified or revoked. Modification or revocation may be effected by a notice to the taxpayer to whom the ruling originally was issued, or by a Revenue Ruling or other statement published in the Internal Revenue Bulletin.

(5) Except in rare or unusual circumstances, the revocation or modification of a ruling will not be applied retroactively with respect to the

> taxpayer to whom the ruling was originally issued or to a taxpayer whose tax liability was directly involved in such ruling if x x x
>
> > (v) the taxpayer directly involved in the ruling acted in good faith in reliance upon the ruling and the retroactive revocation would be to his detriment.
>
> xxx xxx xxx
>
> (7) If a ruling is issued covering a continuing action or a series of actions, and it is determined that the ruling was in error or no longer in accord with the position of the Service, the Commissioner ordinarily will limit the retroactivity of the revocation or modification to a date not earlier than that on which the original ruling was modified or revoked." (Vol. 9, Mertens, Law of Federal Income Taxation, Chap. 49, pp. 146-147.)

Under the above quoted Section (4), the two ways by which the modification or revocation of a ruling may be effected are (1) by a notice to the taxpayer to whom the ruling was originally issued; or (2) by a revenue ruling or other statement published in the Internal Revenue Bulletin.

As borne by the records, Revenue Memorandum Order No. 15-72 was not published in the Official Gazette and it was not addressed to petitioner nor was petitioner furnished a copy or notified thereof until respondent sent the revised and reduced assessment dated July 17, 1986 on July 29, 1986 (Exh. "E") where he advised petitioner of the existence of said Order for the first time. (t.s.n., pp. 30-31, April 1, 1987.) Since Revenue Memorandum Order No. 15-72 was never published and neither was petitioner ever notified of its existence until the issuance of the revised assessment on July 17, 1986, it seems clear that said Revenue Memorandum Order dated May 17, 1972 could not have effected the revocation or reversal of the ruling issued to petitioner on July 3, 1969. (See **Sy Man vs. Jacinto**, 93 Phil. 1093; **People vs. Que Po Lay**, 94 Phil. 640; **Lim Hoa Sing vs. Central Bank**, 104 Phil. 573.)

As mentioned earlier, petitioner was never notified of any revocation or reversal of the July 3,1969 ruling until the issuance of the deficiency income tax assessment involved herein on March 30, 1984. It is thus clear beyond doubt that the said deficiency assessment is a retroactive application of the revocation of said July 3, 1969 ruling which would be prejudicial to petitioner in violation of Section 338-A (now Section 278) of the National Internal Revenue Code. Consequently, the decision of respondent holding petitioner Philippine Long Distance Telephone Company liable for deficiency income taxes in the amount of P495,425,391.00 for the years 1969 to 1980 cannot be sustained, notwithstanding our finding with respect to the first issue that petitioner's income tax exemption has not been restored.

WHEREFORE, the judgment under review should be as it is hereby reversed. No costs.

SO ORDERED.

Quezon City, Metro Manila, December 28, 1988.

AMANTE FILLER
Presiding Judge

ALEX Z. REYES
Associate Judge

CONSTANTE C. ROAQUIN
Associate Judge

C E R T I F I C A T I O N

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

AMANTE FILLER
Presiding Judge
Court of Tax Appeals