REPUBLIC OF THE PHILIPPINES
Court of Tax Appeals
QUEZON CITY

Second Division

SMART COMMUNICATIONS INC.,
Petitioner,

-versus-

PROVINCE OF CAGAYAN and LILIA M. LACAMBRA, in her capacity as OIC-Provincial Treasurer of the Province of Cagayan,
Respondents.

CTA AC NO. 291
(Civil Case No. 8456)

Members:

RINGPIS-LIBAN, *Chairperson,*
MODESTO-SAN PEDRO, and
FERRER-FLORES, *JJ.*

Promulgated:

FEB 27 2025 1:15 pm

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DECISION

MODESTO-SAN PEDRO, J.:

The Case

This is a Petition for Review[1] under *Section 11*, in relation to S*ection 7(a)(3), Republic Act (R.A.) No. 1125*, as amended by *R.A. No. 9282* and *R.A. No 9503*, to appeal the Decision, dated November 29, 2021 (the "Assailed Decision"), and Resolution dated April 20, 2023 (the "Assailed Resolution"), of the Regional Trial Court, Tuguegarao City, Branch 10 (the "RTC" or the *court a quo*) in Civil Case No. 8456, which dismissed petitioner Smart Communications Inc.'s judicial protest against respondent Province of Cagayan's local franchise tax assessments for the calendar years ("CY") 2011 to 2015 in the aggregate amount of Forty-Eight Million Five Hundred Eighty-Seven Thousand Four Hundred Ninety-Seven and 20/100 Pesos (Php48,587,497.20).

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[1] *Rollo*, pp. 5 to 43.

The Parties

Petitioner Smart Communications Inc. is a domestic corporation existing under and by virtue of the laws of the Republic of the Philippines, with principal office address at SMART Tower, 6799 Ayala Avenue, Makati City Philippines.

Respondent Province of Cagayan is a local government unit organized and existing under the laws of the Philippines and in accordance with the *Local Government Code of 1991* (the "LGC") with its office address at the Cagayan Provincial Capitol, Tuguegarao City; while respondent Lilia M. Lacambra is the Officer-in-Charge ("OIC") at the Office of the Provincial Treasurer, Province of Cagayan.

The Facts

Petitioner received on May 13, 2016, a Letter from respondent dated April 29, 2016, with attached computation and assessment, demanding payment of franchise tax from the CY 2011 to 2015 in the total amount of Php48,587,497.20.

Petitioner filed a protest to said Letter on June 7, 2016, but this was not acted upon by respondent Lacambra, prompting petitioner to file an appeal before the RTC.

The RTC dismissed the appeal for lack of jurisdiction, explaining that *Batas Pambansa Blg. 129* does not confer appellate jurisdiction on the RTC over rulings made by non-judicial entities, such as respondent Province. After petitioner's motion, the RTC reconsidered and eventually ruled on the case's merits and the parties' arguments but still ended up denying petitioner's appeal.

Thereafter, petitioner filed its Petition for Review with this Court on May 24, 2023,[2] to which respondents posted their Comment[3] on October 4, 2023, within the extended time granted by the Court.

On February 12, 2024, the RTC elevated the case records of the above-captioned case to this Court.[4] γ

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2 *Id.*
3 *Id.* at 217 to 223.
4 See Tranmittal of Atty. Albine Hyacinth S. Diaz, *id.* at 257.

Following the parties' filing of their respective Memoranda on December 14, 2023 for petitioner,[5] and February 15, 2024 for the respondents,[6] this case was submitted for decision on February 27, 2024.[7]

The Issues

Petitioner submitted the following issues for this Court's consideration:

A. The RTC erred in not holding that respondent's right to assess petitioner for local franchise tax for CY 2011 is already barred by prescription;

B. The RTC erred in holding that under petitioner's legislative franchise, which contains a "in lieu of all taxes" clause, local franchise tax may nevertheless be imposed on petitioner by respondent province;

C. The RTC erred in not holding that petitioner is exempt from local franchise tax under the equality clause of the *Public Telecommunications Policy Act*;

D. The RTC erred in holding that the passage of the *Expanded Value-Added Tax Law* ("E-VAT Law") rendered "in lieu of all taxes" clause in petitioner's legislative franchise *functus officio*;

E. Even assuming that petitioner is liable for local franchise tax, the RTC erred in not holding that respondent province cannot impose local franchise tax in view of the City of Tuguegarao's exclusive jurisdiction to impose the same;

F. Even assuming that petitioner is liable for local franchise tax, respondent's assessment for local franchise taxes for CYs 2011 to 2015 is null and void due to the absence of an examination of petitioner's books of accounts and other records; and

G. The RTC erred in not holding that respondent province's assessment and computation of local franchise tax lack legal and factual bases.

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[5] *Id.* at 227 to 255.
[6] *Id.* at 260 to 266.
[7] Minute Resolution dated February 27, 2024, *id.* at 137.

Arguments of the Parties

Petitioner's Arguments[8]

Petitioner's arguments can be summarized as follows:

1. Respondent province's right to assess petitioner for local franchise tax for CY 2011 is barred by prescription in accordance with *Section 194 of the LGC* and *Section 133 of the Revised Revenue Code of the Province of Cagayan ("Cagayan Revenue Code")*.

2. Petitioner's was granted a legislative franchise by the Congress through the enactment of *R.A. No. 7294*, and *Section 9* thereof provides that petitioner shall be liable to pay franchise tax equivalent to 3% of its gross receipts, which shall be in lieu of all taxes on the franchise or earnings thereof.

3. The *Public Telecommunications Policy Act* (*"PTPA"*) serves to exempt petitioner from payment of local taxes by virtue of *Section 23* thereof, according equality of treatment in the telecommunications industry in that any exemption thereafter granted shall ipso facto become part of previously granted telecommunications franchises. In this respect, petitioner invokes that it enjoys the same privilege extended to Globe Mackay and Radio Corporation's ("Globe") legislative franchise being granted with gross receipts tax "in lieu of all taxes".

4. The *E-VAT Law* did not render *Section 9 of R.A. 7294* functus officio as the repealing clause in the former only pertains to the rates of franchise taxes.

5. Respondent's assessment for local franchise tax is null and void since petitioner is outside respondent's territorial jurisdiction pursuant to *Article 226 of the Implementing Rules and Regulations ("IRR")* of the *LGC*.

6. Assuming respondent may impose local franchise tax on petitioner, the same is still null and void for failure of respondent to conduct the examination of petitioner's books of accounts and records pursuant to *Section 171 of the LGC*, *Section 259 of its IRR*.

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[8] Petitioner's Memorandum, *id.* at 232 to 253.

7. Respondent's assessment of local franchise tax lacks factual and legal bases as it had no authority to assess the alleged tax on the basis of "estimated load per month" and its presumed market share.

Respondent's Counter-argument[9]

Respondent insists that petitioner is liable for the local franchise tax by virtue of *Section 137 of the LGC*, in relation to *Section 2G.02 of the Cagayan Revenue Code of 2005*, considering that petitioner's business is being conducted in the whole province of Cagayan and not just in the City of Tuguegarao. Also, petitioner's franchise tax was already abolished by the *E-VAT Law*, with petitioner now being subjected to VAT.

The Ruling of the Court

After going through the arguments raised by the parties, the Court finds good ground to grant the Petition for Review.

Petitioner is not exempt from local franchise tax

Petitioner insists on its entitlement to an exemption from paying local franchise tax by virtue of its legislative franchise under *R.A. 7294*, where *Section 9* thereof provides that it shall pay a franchise tax of 3% of all gross receipts and said percentage shall be "in lieu of all taxes", to wit:

> SECTION 9. *Tax provisions.* — The grantee, is 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 and italics, Ours.) p

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[9] Respondent's Memorandum, *id.* at 216 to 265.

However, petitioner faults respondent for ruling against the foregoing claim by relying on a Separate Opinion of Retired Supreme Court Associate Justice Antonio T. Carpio in the case of *Philippine Long Distance Telephone Company, Inc. vs. City of Davao*[10] ("*PLDT case*") that the "in lieu of all taxes" in PLDT's legislative franchise applies only to national internal revenue taxes and not to local taxes and that the abolition of the franchise tax on telecommunications companies and its replacement by the VAT effective January 1, 1996 has rendered ineffective the "in lieu of all taxes" clause in the franchise of Smart.

The issue herein is no longer novel. In two instances, the Supreme Court has already ruled that petitioner is not exempted from payment of local franchise tax. Both in the *City of Iloilo, et. al. vs. Smart Communications, Inc.*[11] (*City of Iloilo case*) and *Smart Communications, Inc. vs. The City of Davao, et. al.,*[12] (*City of Davao case*) the High Court consistently ruled that the "in lieu of all taxes" clause applies only to national internal revenue taxes and not to local taxes and even cited Justice Carpio's separate opinion in the *PLDT case* in explaining such ruling.

Thus, contrary to petitioner's claim, even if respondent relied on a separate opinion in a different case, the principle embodied in said opinion had already become a binding jurisprudence when it was relied upon in two succeeding cases, as cited above, especially involving petitioner itself. In fact, the arguments of petitioner in the above cases are the same as the arguments it brought forth in this case. Further, there were no other jurisprudence overturning said cases. We consequently see no reason to deviate therefrom.

Petitioner further posits that such interpretation is erroneous and insists that the "in lieu of all taxes" clause in *Section 9 of R.A. 7294* intended to include local taxes in the exemption by mentioning that it shall still be "liable to pay the same taxes on their real estate, buildings and personal property . . . as other persons or corporations which are now or hereafter may be required by law to pay."

The Court cannot subscribe to said interpretation.

Verily, the uncertainty in the "in lieu of all taxes" clause in *R.A. No. 7294* on whether petitioner is exempted from both local and national franchise tax is construed strictly against it, considering that it is claiming an exemption. Petitioner has the burden of proving that, aside from the imposed 3% franchise tax, Congress intended it to be exempt from all kinds of franchise taxes — whether local or national. However, petitioner failed in this regard.

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[10] G.R. No. 143867 (Resolution), March 25, 2003.
[11] G.R. No. 167260, February 27, 2009.
[12] G.R. No. 155491, September 16, 2008.

The alleged grant, by law, of a tax exemption must be clear and concise. It must be unequivocal and not inferred. Petitioner's attempt to introduce a new interpretation cannot be sustained as it entails mere inferring that the mere mention of a particular type of local tax is tantamount to an intention to include all local taxes.

It is hornbook doctrine that tax exemptions are strictly construed against the claimant. For this reason, tax exemptions must be based on clear legal provisions, not by mere inference. Since, as held in the *PLDT, City of Iloilo and City of Davao cases*, the law granting franchise in favor of petitioner does not clearly state so, local taxes cannot be interpreted as to be included in the "in lieu of all taxes" clause of *Section 9 of R.A. 7294*.

Anent the *E-VAT Law*, petitioner posits that *Section 20*[13] thereof only amended the tax rates but did not remove its tax exemption. As clarified in *Revenue Memorandum Circular ("RMC) No. 05-96*, the VAT merely replaced the franchise tax, but the "in lieu of all taxes" benefits under its legislative franchise still stand.

Again, such argument is misplaced.

Q&A No. 4 of *RMC No. 05-96* clarified that the "in lieu of all taxes" provision in the franchise is not affected by the *E-VAT Law*. VAT merely replaced the franchise tax. In other words, VAT instead of franchise tax shall be in lieu of all taxes due from a franchise grantee.

To Our mind, this clarification is only a matter of terminologies and rates with respect to the kind of tax and the rate applicable. The jurisprudential principle and interpretation of the "in lieu of all taxes" clause in the franchise remains, as shown by the RMC's use of the term "is not affected". As such, we return to the prevailing stand that "in lieu of all taxes" does not include local taxes, as already discussed above.

Defeated on this aspect, petitioner, again, invokes the equality clause under *Section 23 of the PTPA (R.A. 7925)*, which states:

> SEC. 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. ɣ

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[13] Section 20. *Repealing Clauses.* — The provisions of any special law *relative to the rate of franchise taxes* are hereby expressly repealed. (Italics, Ours.)

In this regard, petitioner cites the legislative franchise granted to Globe under *R.A. 7227*, where *Section 9(b)* thereof states that "the grantee shall further pay to the Treasurer of the Philippines each year after the audit and approval of the accounts as described in this Act, one and one-half percentum of all gross receipts from business transacted under this franchise by the said grantee in the Philippines, *in lieu of any and all taxes of any kind, nature or description levied, established or collected by an authority whatsoever, municipal, provincial or national*, from which the grantee is hereby expressly exempted . . ."

This matter has already been resolved as early as in the *PLDT case* and in *Digital Telecommunications Philippines, Inc. vs. Province of Pangasinan*[14] ("*Digitel case*"). The language of *Section 23 of R.A. No. 7925* and the proceedings of both Houses of Congress are bereft of anything that would signify the grant of tax exemptions to all telecommunications entities, including those whose exemptions had been withdrawn by *R.A. No. 7160*. The term "exemption" in *Section 23 of R.A. No. 7925* does not mean tax exemption. The term refers to exemption from certain regulations and requirements imposed by the National Telecommunications Commission. The thrust of the PTPA 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 same has been upheld in the *City of Iloilo and City of Davao cases*, further explaining that an 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. The Court does not find any reason to deviate from the same.

All told, petitioner's insistence on its local franchise tax exemption is untenable. However, as discussed hereunder, respondent's local franchise tax assessment must still fail.

The local franchise tax assessment for the year 2011 has already prescribed

Petitioner posits that out of the total local franchise tax assessment of ₱48,587,497.20 for the years 2011 to 2015, the amount of ₱10,347,823.73 arising from 2011 has already prescribed based on *Section 194 of the LGC* and *Section 133 of the Cagayan Revenue Code*. Considering that the demand letter for payment was received by petitioner only on May 13, 2016, the local franchise tax assessed for the year 2011 already prescribed.

[14] G.R. No. 152534, February 23, 2007.

Petitioner is correct.

Section 166 of the LGC provides that unless otherwise provided, all local taxes, fees, and charges shall accrue on the first (1^{st}) day of January of each year. Further, *Section 167* of the same states that unless otherwise provided, *all local taxes*, fees, and charges *shall be paid within the first twenty (20) days of January* or of each subsequent quarter, as the case may be.

Meanwhile, *Section 194 of the LGC* provides that local taxes, fees, or charges shall be assessed within five years from the date they became due. No action for the collection of such taxes, fees, or charges, whether administrative or judicial, shall be instituted after the expiration of such period. The same is replicated in *Section 133 of the Cagayan Revenue Code*. Respondent thus only had five years from the date the tax became due within which to assess the same.

Since local taxes for the year 2011 became due for payment on January 20, 2011, in accordance with *Section 167 of the LGC*, respondent had until January 20, 2016 to assess the same. Respondent's power to assess local franchise tax for the year 2011, however, had already prescribed when petitioner received the demand letter on May 13, 2016.

The assessment against petitioner for the year 2011 is thus void due to prescription.

Respondent is not authorized to impose local franchise tax outside its territorial jurisdiction

Petitioner asserts that respondent has no authority to impose and collect local franchise tax since petitioner is operating within Tuguegarao City, which is outside respondent's jurisdiction, pursuant to *Section 137 of the LGC* and *Article 226 of its IRR*.

On this score, respondent counters that *Article 226 of the LGC IRR* applies only to businesses enjoying a franchise that operate their business within the confines of a city only and not when the business extends beyond the territorial limits of a city as in the case of petitioner. Petitioner's telecommunications operations does not only take place within the territorial jurisdiction of Tuguegarao City. The extent and scope of petitioner's business activities in the Province of Cagayan are evident through the installation and maintenance of cellular towers in various municipalities within the province. As such, the gross receipts should not be considered as earned solely within its Tuguegarao City office where bill payments are processed. Instead, the gross receipts or income should be attributed to the place where the services were actually used, enjoyed, or availed of by petitioner's subscribers.

We find that petitioner's franchise operations are outside respondent Province's territorial jurisdiction.

Section 137 of the LGC authorizes the province to impose a tax on businesses enjoying a franchise at a rate not exceeding 50% of 1% of the gross annual receipts for the preceding calendar year based on the incoming receipt, or realized, *within its territorial jurisdiction.*

However, *Article 266(b) of the LGC's IRR* clarified that the province shall not impose the tax on business enjoying franchise operating within the territorial jurisdiction of any city located within the province.

The *LGC* does not expressly provide guidelines for determining the situs of a local franchise tax. However, we can take a cue from *Section 150(a) of the LGC* which states that for purposes of collection of the taxes under *Section 143* of said Code, manufacturers, assemblers, repackers, brewers, distillers, rectifiers and compounders of liquor, distilled spirits and wines, millers, producers, exporters, wholesalers, distributors, dealers, contractors, banks and other financial institutions, and other businesses, maintaining or operating branch or sales outlet elsewhere *shall record the sale in the branch or sales outlet making the sale or transaction, and the tax thereon shall accrue and shall be paid to the municipality where such branch or sales outlet is located.*

From this, we can deduce the LGC's basis in determining situs of taxation is on where the sale is recorded. *Section 137 of the LGC* provides that the franchise tax is imposed on incoming receipts. Accordingly, local franchise tax is imposed on where the receipts are recorded, regardless of where the service which generated the gross receipts is realized.

In this case, it is undisputed that petitioner's gross receipts are recorded in Tuguegarao City. As such, pursuant to *Article 266(b) of the LGC IRR*, petitioner's gross receipts are already outside respondent's territorial jurisdiction.

Consequently, respondent cannot impose local franchise tax thereon.

Respondent's local franchise tax assessment is void

Petitioner anchors the invalidity of the local franchise tax assessment for the years 2011 to 2015 on the following grounds:

a.) Respondent did not conduct an examination of petitioner's books of accounts and other records; and b.) Respondent is not authorized to use alleged manner of computation – Presumptive Level Income Assessment Approach ("PLIAA") – in coming up with the assessment.

Respondent's Computation of Franchise Tax of petitioner is as follows:

Cagayan Population		729,542
Estimated Load per Month	Php	300.00
		12
Annual Presumptive Gross Receipts		2,626,351,200.00
Estimated Market Share		40%
Annual Estimated Share		1,050,540,480.00
Franchise Tax (%)		0.005
Total Amount Due		5,252,702.40

Notably, the above computation is the same for the years 2011 to 2015. The total assessed amount due differed merely on the interest and surcharges each year.

While the manner in which the assessment and its computation were issued was not discussed during trial in the court *a quo*, this Court cannot turn a blind eye to a blatant naked assessment.

First, the source/s of the numerical data (i.e. Cagayan Population, the Estimated Load per Month, and Estimated Market Share) used by respondent in its computation cannot be verified.

Second, and more glaringly so, these numerical data remained exactly the same for the years 2011 to 2015, which to the Court's mind is not factually feasible.

While respondent, as a government authority, enjoys the presumption of regularity in the performance of its duties and that tax assessments are *prima facie* correct, the same cannot apply to an assessment that is without foundation or are arbitrary and capricious.

The rule is that in the absence of the accounting records of a taxpayer, its tax liability may be determined by estimation. In other words, respondent is not required to compute such tax liabilities with mathematical exactness—approximation in the calculation of the taxes due is justified. To hold otherwise would be tantamount to holding that skillful concealment is an invincible barrier to proof. *p*

However, the rule does not apply where the estimation is arrived at arbitrarily and capriciously.[15] Where the BIR has come out with a "naked assessment," i.e., without any foundation character, the determination of the tax due is without rational basis.[16] The same rule must apply to all taxing authorities, including local government units like respondent.

With the foregoing considered, respondent's local franchise tax assessment is void and must thus be cancelled.

ACCORDINGLY, the instant Petition for Review is **GRANTED**.

The November 29, 2021 Decision and April 20, 2023 Resolution of the Regional Trial Court of Tuguegarao City, Branch 10 in Civil Case No. 8456 is **REVERSED** and **SET ASIDE**. Accordingly, the assessment made by respondents against petitioner for alleged local franchise taxes for the years 2011 to 2015 in the total amount of Forty-Eight Million Five Hundred Eighty-Seven Thousand Four Hundred Ninety-Seven and 20/100 Pesos (Php48,587,497.20) is hereby **CANCELLED** and **SET ASIDE**. Consequently, respondents are **ENJOINED** and **PROHIBITED** from collecting the said amount against petitioner.

SO ORDERED.

MARIA ROWENA MODESTO-SAN PEDRO
Associate Justice

WE CONCUR:

MA. BELEN M. RINGPIS-LIBAN
Associate Justice

CORAZON G. FERRER-FLORES
Associate Justice

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15 *Commissioner of Internal Revenue vs. Hantex Trading Co., Inc.*, G.R. No. 136975, March 31, 2005.

16 *Id.*

ATTESTATION

I attest that the conclusions in the above Decision were reached in consultation before the case was assigned to the writer of the opinion of the Court's Division

MA. BELEN M. RINGPIS-LIBAN
Associate Justice
Chairperson

CERTIFICATION

Pursuant to Article VIII, Section 13 of the Constitution and the Division Chairperson's Attestation, it is hereby certified that the conclusions in the above Decision were reached in consultation before the case was assigned to the writer of the opinion of the Court.

ROMAN G. DEL ROSARIO
Presiding Justice