REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

CAGAYAN ELECTRIC POWER & LIGHT COMPANY, INC.,
Petitioner,

- versus -

C.T.A. CASE NO. 5883

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated:
MAY 04 2001

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DECISION

The instant petition seeks the issuance of a tax credit certificate in favor of the Petitioner in the amount of P4,216,419.00 allegedly representing erroneously paid value-added taxes (VAT) on its importations of equipment, machinery and spare parts from May 1997 to October 1998.

The factual backdrop of the case are as follows:

Petitioner is a corporation duly formed and existing under and by virtue of the laws of the Philippines, with principal offices at the 8th Floor, Strata 100 Building, Emerald Avenue, Ortigas Center, Pasig City.

On June 17, 1961, Petitioner was granted a legislative franchise under Republic Act No. 3247 "to construct, maintain and operate an electric light, heat and power system for the purpose of generating and/or distributing electric light, heat and/or power for sale within the City of Cagayan de Oro and its suburbs. The grantee shall further have the right and privilege to install, lay and maintain on all streets, public thoroughfares, bridges and public places within said limits, poles, wires, transformers, capacitors, overhead protective devices, and pole line hardware, and other equipment necessary for the safe distribution of electric current to the public."

Said franchise was amended on June 21, 1963 by Republic Act No. 3570 to include the municipalities of Tagoloan and Opol, both in the Province of Misamis Oriental, to Petitioner's areas of operation and was further amended on August 4, 1969 by Republic Act No. 6020 to include the municipalities of Villanueva and Jasaan, also in the Province of Misamis Oriental.

From May 1997 to October 1998, Petitioner imported from different countries various equipment, machinery and spare parts necessary in the conduct of its business and was required to pay VAT in the aggregate amount of P4,216,419.00. Petitioner, however, claims that Respondent should not have collected VAT on its importation, citing Section 3 of Republic Acts 3247, 3570 and 6020 which uniformly provide:

> "**Section 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 city treasury of Cagayan de Oro: **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.**"

Thus, on April 8, 1999, Petitioner filed a letter-claim for the refund of the amount of P4,216,419.00 (Exhibit ZZZ) anchored on the following grounds:

A. Sections 108 and 109 of the NIRC specifically excludes electric franchisees from coverage of the value-added tax;

B. In BIR Ruling 46-97, the Honorable Commission (sic) of Internal Revenue ruled that an electric franchisee is exempt from value-added tax;

C. The Court of Tax Appeals has held that electric franchisees are exempt from value-added tax on importations; and

D. The Supreme Court has consistently upheld the "in lieu of all taxes" proviso in the franchises of numerous grantees.

As Respondent failed to act on Petitioner's claim and to toll the running of the two-year prescriptive period, the instant petition was filed on May 14, 1999.

In his Answer filed on June 22, 1999, Respondent claimed by way of Special and Affirmative Defenses that:

"4. He reiterates and repleads the preceding paragraphs of this answer as part of his Special and Affirmative Defenses;

5. The Value Added Tax (VAT) on importation under Section 101 of the 1993 Tax Code, as amended, is neither a tax on franchise nor on gross receipts or earnings thereof. It is a tax on the privilege of importing goods whether or not the taxpayer is engaged in business and regardless of whether the imported goods are intended for sale, barter or exchange;

6. An analysis of Sections 1 and 2 of R.A. 3247, as amended by R.A. 3570 and further amended by R.A. 6020, which allegedly governs petitioner's legislative franchise would show that the "right, privilege and authority" conferred to it are limited to the following, to wit:

(a) "x x x to construct, maintain and operate an electric light and power system for the purpose of generating and distributing electric light and power for sale within the municipalities x x x."

(b) "x x x to install, lay and maintain on all streets, public thoroughfares, bridges and public places within said limits, poles,

> wires, transformers, capacitors, overhead protective devices, and poles line hardware and other equipment necessary for the safe distribution of electric current to the public x x x."

Petitioner's alleged exemption from VAT based on its privilege to import is unmistakably not one among those enumerated in the aforequoted rights and privileges. Petitioner's theory of exemption, therefore is a mere opinion, speculation and conclusion bereft of any basis in law.

7. The Supreme Court in the case of Borja vs. Collector of Internal Revenue (3 SCRA 590), ruled that:

> "Considering Section 190 of the Tax Code is a sort of an equalizer, to place casual importers, who are not merchants on equal footing with established merchants who pay sales tax on articles imported by them, a grantee of a legislative franchise is not exempt from the payment of compensating tax on the goods directly imported for use in her electric plant."

A close analysis of the legal principles enunciated in said case reveals that the rationale for the imposition of compensating tax for importation of goods by a franchise-grantee, likewise apply to the Value Added Tax on importation of personal properties. Such being the case, it was not the intention, therefore, of R.A. 3247 as amended by R.A. 3570, and further amended by R.A. 6020, to exempt herein petitioner from payment of Value Added Tax on its importation of certain equipments, machinery, etc., since it does not appear clearly and manifestly in its legislative franchise that an exemption from payment of VAT on its importation was intended. Hence, the legislative franchise allegedly granted to herein petitioner must be construed strictly against the grant of tax exemption.

8. The VAT under Section 101(a) of the .977 (should be 1997 Tax Code) Tax Code, as amended, replaced the advance sales tax and compensating tax under then Sections 162(c) and 169 of the 1977 Tax Code. Accordingly, the 3% franchise tax did not substitute the 10% value added tax on petitioner's importations of equipments, machineries and spare parts for the use of its electric power plant;

9. Exemption from taxation is highly disfavored in law; and he who claims exemption must be able to justify his claim by the clearest grant of organic or statutory law. In other words, an exemption from the common burden cannot be permitted to exist upon vague implication (Asiatic Petroleum Co. vs. Llanes 49 Phil. 466);

10. In an action for refund and/or tax credit, the taxpayer has the burden of showing that the taxes paid were erroneously collected, and failure to sustain this burden is fatal to the action for refund and/or tax credit;

11. Claims for refund and/or tax credit are construed strictly against claimants since they are in the nature of tax exemption. They cannot be allowed unless granted in the most explicit and categorical language. (Manila Electric Co. vs. CIR, 47 SCRA 351);

12. Petitioner must show that it has complied with the provisions of Sections 204(c) and 229 of the 1997 Tax Code on the filing of a written claim for refund within two (2) years from the payment of the tax.

In their Joint Stipulation of Facts and Issues filed before this Court on September 2, 1999, the parties submitted the following issues for resolution:

(A) Whether or not Petitioner is exempt from paying Value-Added Tax on its importations of equipment, machinery and spare parts under Republic Act No. 3247, as amended by Republic Acts Nos. 3570 and 6020.

(B) Whether or not Petitioner's importations of certain equipment, machinery and spare parts for the period May 1997 to October 1998 were made in the course of its business.

(C) Whether or not Petitioner is entitled to tax credit in the total amount of P4,216,419.00 as erroneous payment of Value-Added Tax on its importation made from May 1997 to October 1998.

We find for the Petitioner.

The first issue had long been settled in a number of similar cases brought before Us, the most recent of which is **CTA Case No. 5413 entitled Davao Light and Power Company, Inc. promulgated last August 7, 1998.** In the said case, We ruled that the "in lieu of all taxes" provision includes exemption from the payment of the Value-Added Tax on the importation of equipment, machinery and spare parts, thus:

> "This above issue is not a case of first impression. In the analogous case of Philippine Long Distance Company vs. Commissioner of Internal Revenue, CTA Case No. 5106, promulgated on December 18, 1995, We have already ruled that the "in lieu" provision includes exemption from the payment of VAT on the importation of equipment, machineries and spare parts. We quote:
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> > "The phrase 'in lieu of' means instead of, in place of; or in substitution for (Black v. Barnes, 46 P. 2d 625, 626, 142 Kan. 381; Rutherland v. Oroville-Wyandotte Irr. Dist. 22 P. 2d 505, 218 Cal. 242; Words and Phrases, Vol. 21, p. 472). It does not mean 'in addition to' (Glassman Const. Co. v. Baltimore Brick Co., 246 Md. 478, 228 A.2d 472, 474, Black's Law Dictionary, 6th ed., 1990, p. 787). The 'in lieu of' implies the existence of something for which a substitution is being made. Thus, the 'in lieu of all other taxes' means that none other than the tax specified however described can be demanded. It limits the liability to the specific tax (State of Tennessee v. Bank of Commerce, 53 P. 735, 736, Words and Phrases, Vol. 21, p. 474). Thus, the phrase 'in lieu of all taxes' has the effect of exempting from taxation the VAT which is covered under the general term 'taxes' under Section 12 of R.A. 7082) on the purchases of imported equipments, machineries and spare parts made by petitioner by virtue of its paying of the 3% Franchise Tax pursuant to Section 117 of the NIRC and Section 12 of R.A. 7082. The rationale or purpose for the exemption from all other taxes except the income tax and the real property tax granted on petitioner upon the payment of the 3% Franchise Tax is 'that such exemption is part of the inducement for the acceptance of the franchise and the rendition of public service by the grantee' (Province of Misamis Oriental v. Cagayan Electric Power and Light Company, Inc., G.R. No. 45355, January 12, 1990, 181 SCRA 38). (Underscoring supplied)
>
> (citing **Cotabato Light and Power Company, Inc. vs. The Honorable Commissioner of Internal Revenue, CTA Case No. 5396, dated June 1, 1998**)

Likewise, in the case of **Province of Misamis Oriental vs. Cagayan Electric Power and Light Company, Inc., 181 SCRA 38**, the Supreme Court upheld the validity and effectivity of the "in lieu of all taxes" provision found in Petitioner's legislative franchise and held that the franchise was not amended by PD 231 (Local Tax Code) which authorized provinces to impose franchise tax on businesses operating in the provinces.

We proceed to the second issue. Records show that Petitioner's importations of equipment, machinery and parts for the period of May 1997 to October 1998 were made in the course of its business. The various documents submitted by Petitioner such as Supplier's Invoices, Purchase Orders, Bureau of Customs Import Entry Declarations, Bureau of Customs Import Entry and Internal Revenue Declarations, (Exhibits B to YYY-1, CCCC-1 to CCCC-177, inclusive) as well as the testimony of its Senior Purchasing Officer, Mr. Raul Fernandez, (TSN, September 16, 1999 and March 21, 2000) prove that the items covering its importations for the said period consisted of equipment, machinery and spare parts necessary for the modernization and standard operation of its franchise.

Finally, as to whether or not Petitioner is entitled to tax credit in the amount of P4,216,419.00, after an examination of the evidence adduced by Petitioner, this Court finds that it has sufficiently established that it is entitled to the issuance of a tax credit certificate corresponding to the VAT it erroneously paid on importations from May 1997 to October 1998 but only to the extent of P3,789,748.00.

The SGV & CO, through its Partner, Mr. Ruben R. Rubio, was commissioned by this Court pursuant to CTA Circular 1-95, as amended, to verify Petitioner's claim for refund. In his report dated February 10, 2000 (Exhibit AAAA), he certified that out of Petitioner's total claim for refund of P4,216,419.00, the amount of P411,350.00 was not properly substantiated (Exhibit AAAA-1). Thus, the said auditing firm disclosed that only the amount of P3,805,069.00 was properly supported by Import Entry Declarations and Bureau of Customs (BOC) Official Receipts stamped "Certified Xerox Copy" or "Certified True Copy" and signed by the BOC.

Upon further verification, however, this Court finds that the value-added tax of P15,321.00 paid on April 22, 1997 as can be seen in the BOC Import Entry & Internal Revenue Declaration (Exhibits CCCC-38 & CCCC-39) is already barred by prescription and should also be excluded from Petitioner's claim. Inasmuch as Petitioner filed its administrative and judicial claims for refund on April 8, 1999 (Exhibit ZZZ) and May 14, 1999, respectively, any VAT payment made by Petitioner prior to May 14, 1997 is considered not within the two-year period prescribed under Section 230 (now Section 229) of the Tax Code. Therefore, We reduce the SGV recommended amount of P3,805,069.00 by P15,321.00 resulting to a net amount of P3,789,748.00.

In his Memorandum, Respondent raised the following arguments: first, that Petitioner's privilege to import goods is unmistakably not one among those rights and privileges enumerated in its legislative franchise; thus, Petitioner's alleged exemption from VAT is without any basis in law; second, that even if Petitioner is exempt from VAT, it is not entitled to the refund of input taxes on capital goods provided under

Section 4.106-1(b) of Revenue Regulations No. 7-95 and third, that VAT paid prior to May 14, 1997 was already barred by prescription.

The first argument raised by Respondent was passed upon by this Court also in the case of **Cotabato Light and Power Company, Inc. vs. The Honorable Commissioner of Internal Revenue,** *supra*, where We ruled that the right to construct and maintain an electric light, heat and power system impliedly includes the right to import the necessary equipment, machinery and spare parts. Pertinent portions of the said decision are quoted hereunder:

> "Most importantly, a close reading of Sections 1 and 2 of Act No. 3636 together with Commonwealth Act No. 487 and Republic Act No. 3341 which govern petitioner's legislative franchise would show that the "right, privilege and authority" conferred to it to construct and maintain an electric light, heat and power system necessarily includes the importation of transformers and spare parts for engine and turbo charger, thus:
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> > a) ". . . to construct, maintain, and operate an electric light, heat, and power system for the purpose of generating and distributing electric light, heat, and power, for sale within the limits of the municipality (or municipalities. . .)"
> >
> > b) ". . . to install, lay, and maintain in, along, under, and over all public property of the municipality (or municipalities), including the public streets and highways, provincial roads, bridges, and public squares within said municipality (or municipalities) all necessary apparatus and appurtenances for the transmission and distribution of electric current, and to supply, sell, and furnish such current to any individual, co-partnership, private, public or quasi-public association, corporation, or joint-stock company, within the limits of said municipality (or municipalities) for insular, provincial, municipal, domestic or manufacturing uses or for any other use to which electricity may be put, and to charge and collect a schedule of prices and rates for the use of electric current so furnished, which schedule of prices and rates shall be at all times be subject to regulation by the Public Service Commission"

The word "maintain" has been defined as meaning to bear the expense of; to support; to keep up; to supply with what is needed. (Alzona vs. Vicuña, 41764-R, February 17, 1976 as cited in Moreno's Philippine Law Dictionary, 3rd ed., Alexander vs. Parker, 33 N.E. 183, 184, 144 Ill. 355, 19 L.R.A. 187, citing Webst. Dict., as cited in Words and Phrases) Also, Merriam-Webster Dictionary defines the word "construct" as signifying to "build" or to "make".

From the above definitions, We can readily see that petitioner's acquisition from abroad (or even in the domestic market) is but a part of its right and privilege to construct and maintain an electric light, heat and power system within its franchise area. More specifically, the acquisition is for the purpose of supplying the things needed in the pursuit of such right and privilege.

Petitioner has been given the right and privilege to maintain its franchise operation and this, We believe, also entails the bearing of expenses attendant to its purchase of transformers and spare parts required for construction or maintenance.

If we are to declare such acquisition as not falling within the rights and privileges granted to it, then we are naively defeating or declaring as hollow the very essence of the word "construct" or "maintain" as stated in said law.

It is here where the doctrine of necessary implication applies. "Every statute is understood, by implication, to contain all such provisions as may be necessary to effectuate its object and purpose, or to make effective rights, powers, privileges of jurisdiction which it grants, including all such collateral and subsidiary consequences as may be fairly and logically inferred from its terms[2]. *Ex necessitate legis*. And every statutory grant of power, right or privilege is deemed to include all incidental power, right or privilege. This is so because the greater includes the lesser, expressed in the maxim, *in eo plus sit, simper inest et minus*[3]. "(Statutory Construction by Agpalo, 2nd ed., pp. 117-118)

While it is true that as a rule tax exemptions are strictly construed and highly disfavored in law, as respondent insists, We believe, however, that the case at bar presents an exception because herein petitioner "falls within the purview of exemption by clear legislative intent" (Commissioner of Internal Revenue vs. Arnoldus Carpentry Shop, 159 SCRA 199) The words "maintain" and "construct" provided in the rights and privileges of the petitioner under Sections 1 and 2 of its franchise unmistakably include, by their definition, petitioner's purchase of transformers and spare parts for engine and turbo charger."

Anent Respondent's second argument, it should be noted that the refund or tax credit of input tax on capital goods provided under Section 4.106-1(b) of Revenue Regulations No. 7-95 (implementing Section 106(b) [now Section 112(B)] of the Tax Code) is a privilege given to a VAT-registered person and is not applicable to herein Petitioner, and We quote thus:

SEC. 4.106-1. ***Refunds or tax credits of input tax.*** - x x x

(b) Capital Goods. - Only a VAT-registered person may apply for issuance of a tax credit certificate or refund of input taxes paid on capital goods imported or locally purchased. The refund shall be allowed to the extent that such input taxes have not been applied against output taxes. The application should be made within two (2) years after the close of the taxable quarter when the importation or purchase was made.

Refund of input taxes on capital goods shall be allowed only to the extent that such capital goods are used in VAT taxable business. If it is also used in exempt operations; the input tax refundable shall only be the ratable portion corresponding to the taxable operations.

"Capital goods of properties" refer to goods or properties with estimated useful life greater than one year and which are treated as depreciable assets under Section 29 (f), used directly or indirectly in the production or sale of taxable goods or services.

Based on the tax exemption privileges provided for in its legislative franchise, Petitioner is claiming refund of the VAT imposed to every importer of goods under Section 101(a) [now Section 107(A)] of the Tax Code which provides:

Section 101. ***Value-added tax on importation of goods.*** - (a) *In general.* - There shall be levied, assessed and collected on every importation

> of goods a value-added tax equivalent to 10% based on the total value used by the Bureau of Customs in determining tariff and customs duties, plus customs duties, excise taxes, if any, and other charges, such tax to be paid by the importer prior to the release of such goods from customs custody: Provided, that where the customs duties are determined on the basis of the quantity or volume of the goods, the value-added tax shall be based on the landed cost plus excise taxes, if any.

Clearly, Section 106-1(b) of RR 7-95 cited by Respondent is irrelevant to the case at bar.

Finally, as correctly observed by Respondent, part of Petitioner's claim for refund had already prescribed pursuant to Section 230 (now Section 229) of the Tax Code. Consequently, the amount of P15,321.00 should be disallowed for having been paid on April 22, 1997 (Exhibits CCCC-38 & CCCC-39).

WHEREFORE, in the light of all the foregoing, the instant Petition for Review is hereby **PARTIALLY GRANTED**. Respondent is hereby **ORDERED** to **ISSUE A TAX CREDIT CERTIFICATE** in favor of the Petitioner in the amount of P3,789,748.00 representing erroneously paid VAT on its importations for the period May 14, 1997 to October 1998.

SO ORDERED.

AMANCIO Q. SAGA
Associate Judge

I CONCUR:

ERNESTO D. ACOSTA
Presiding Judge

CERTIFICATION

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

ERNESTO D. ACOSTA
Presiding Judge