REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

MANILA ELECTRIC COMPANY,
Petitioner,

-versus- C.T.A. CASE No. 1737

COMMISSIONER OF INTERNAL REVENUE,
Respondent.
x- - - - - - - - - - - - - - x

Nov. 28/69

D E C I S I O N

Petitioner appealed from the decision of respondent assessing against and demanding from petitioner payment of ₱73,727.34 and ₱80,342.30, or a total of ₱154,069.64, as deficiency income taxes and interests for 1960 and 1961, respectively.

Before this case was heard, the contending parties submitted to this Court an agreed statement of facts as follows:

1. That the petitioner is a corporation duly organized and existing under and by virtue of the laws of the Philippines, with principal office at 900 San Marcelino St., Manila, while the respondent is the duly appointed and qualified Commissioner of Internal Revenue with office at the Department of Finance Building, Manila;

2. That the petitioner filed its income tax return (a) for the calendar year 1960, on April 17, 1961; (b) for the calendar year 1961, on April 13, 1962; and (c) on July 11, 1962, it filed an amended income tax return for 1961;

3. That in an investigation conducted by examiners of the respondent, it was

ascertained that petitioner did not pay corporate income tax on its income from rent of electrical properties, interest and other miscellaneous electrical revenue listed hereunder:

Income Treated under Legislative Franchise	1960	1961
Rent of Electrical Property	₱188,872.00	₱200,114.00
Interest	26,798.00	31,788.00
Miscellaneous Electrical Revenue	34,254.00	40,444.00
Total	₱249,924.00	₱272,346.00

4. That respondent sent to petitioner a letter of demand, dated December 20, 1965, together with assessment notices, which was received by the petitioner on January 28, 1966, demanding the payment of the amounts ₱73,727.34 and ₱80,342.30 or a total amount of ₱154,069.64, as deficiency income tax for 1960 and 1961 computed as follows:

Net income per return	₱1,136,290.00
Add: Revenue not covered by franchise tax and subject to income tax:	
1. Rent of electric property	188,872.00
2. Interest income ...	26,798.00
3. Miscellaneous electric revenue	34,254.00
Net income per investigation	₱1,386,214.00
Tax due thereon	407,864.00
Less: Amount already assessed	332,887.00
Balance	74,977.00
Less: Franchise tax payment	12,496.20
Total ----------------	62,480.80
Add: ½% monthly interest from 4-18-61	

to 4-18-64	₱11,246.54
TOTAL AMOUNT DUE & COLLECTIBLE	₱73,727.34

AGR-301912-65/61

Net income per return	₱1,451,814.00
Add: Revenue not covered by franchise tax and subject to income tax:	
1. Rent of electrical property	200,114.00
2. Interest income ...	31,788.00
3. Miscellaneous electric revenue	40,444.00
Net income per investigation	₱1,724,160.00
Tax due thereon	509,248.00
Less: Amount already assessed	427,544.00
Balance	81,704.00
Less: Franchise tax payment	13,617.30
Total	68,086.70
Add: ½% monthly interest from 4-17-62 to 4-17-65	12,255.60
TOTAL AMOUNT DUE & COLLECTIBLE	₱80,342.30
GRAND TOTAL	₱154,069.64

5. That the petitioner, through its Comptroller, E. V. Villanueva, sent a letter, dated February 1, 1966, to the respondent, protesting the demand for the payment of deficiency income tax for 1960 and 1961, which letter was received by respondent on February 1, 1966;

6. That the petitioner is an operator of a public utility, engaged in the sale of electricity in Manila and its suburbs under Republic Act No. 150 approved June 14, 1947;

7. That the issues involve in this case are (a) whether the income of petitioner mentioned in paragraph 3 hereof

> is subject to the corporate income tax or the franchise tax provided for in Republic Act No. 150, and (b) whether the inclusion of the ½% monthly interest on the deficiency income taxes for 1960 and 1961 is legal;
>
> 8. That the parties hereby reserve their rights to introduce additional evidence not covered by this Stipulation of Facts in support of their respective contentions. (pp. 44-47, CTA rec.)

The only issue to be resolved in this case is whether or not petitioner is subject to corporate income tax on its income derived from rentals of electrical property, interest and other miscellaneous electrical revenue.

Petitioner contends that the income derived from rentals of its electrical property, interest and miscellaneous electrical revenue is exempt from income tax because it has already paid the franchise tax which, under its legislative franchise, shall be in lieu of all taxes and assessments of any kind and nature whatsoever.

On the other hand, respondent maintains that petitioner's exemption from all taxes and assessments does not extend to extraneous income from rentals of electrical property, interest and miscellaneous electrical revenue. Respondent's position is based on the grounds that (a) petitioner's franchise, Act No. 484 of the Philippine Commission of 1902, as amended by Republic Act No. 150, does not state in clear and express language that petitioner is exempt from all taxes and assessments on income from business not covered by its franchise, and (b) granting arguendo that Act 484 of the Philippine Commission provides that petitioner shall be exempt from all taxes and assessments, it does not state that it shall also be exempt from taxes on its revenues derived from business not covered by its franchise.

The grounds relied upon by respondent are based on his interpretation of Paragraph 9, Part Two, of petitioner's franchise, in relation to Sec. 1 of Republic Act No. 150, which provides as follows:

> Par. 9. The grantee shall be liable to pay the same taxes upon its real estate, buildings, plant (not including poles, wires, transformers, and insulators), machinery and personal property as other persons are or may be hereafter required by law to pay. In consideration of Part Two of the franchise herein granted, to wit, the right to build and maintain in the City of Manila and its suburbs a plant for the conveying and furnishing of electric current for light, heat, and power, and to charge for the same, the grantee shall pay to the City of Manila two and one-half per centum of the gross earnings received from the business under this franchise in the city and its suburbs; Provided, That two and one-half per centum of the gross earnings received from the business of the line to Malabon shall be paid to the Province of Rizal. Said percentage shall be due and payable at the

> times stated in paragraph nineteen of Part One hereof, and after an audit, like that provided in paragraph twenty of Part One hereof, and shall be in lieu of all taxes and assessments of whatsoever nature, and by whatsoever authority upon the privileges, earnings, income, franchise, and poles, wires, transformers, and insulators of the grantee, from which taxes and assessments the grantee is hereby expressly exempted. (Act No. 484 of the Philippine Commission of 1902, as implemented by Mun. Ord. No. 44 of the City of Manila; Underscoring supplied.)

> Section 1. Subject to the provisions of the Constitution of the Philippines and of this Act, and subject further to the Philippine Trade Agreement of 1946, the term of the franchise granted in pursuance to the authority under Act Numbered Four hundred eighty-four of the Philippine Commission by the Municipal Board of the City of Manila to Charles M. Swift, and later assumed and taken over by the Manila Electric Company, as contained in Ordinance Numbered Forty-four, Parts Two and Three, of the said Municipal Board of the City of Manila, as amended, to construct, maintain and operate an electric light, heat and power system for the purpose of generating and distributing for sale electric light, heat and power throughout the City of Manila and its suburbs, is hereby extended, under the same terms and conditions therein provided, for a period of twenty years from the date of its expiration. (Rep. Act No. 150; Underscoring supplied.)

The above franchise of petitioner speaks in clear and unambiguous term that petitioner shall pay the franchise tax in lieu of "all taxes and assessments of whatever nature, and by whatsoever authority upon the privileges, earnings, income, franchise, x x x" for building and maintaining in Manila and suburbs "a plant for the conveying and furnishing for sale of electric current for light, heat and power" in consideration of the payment of "two and one-half per centum of the gross earnings received from its business under this franchise." The amendment introduced by Republic Act No. 150 deals principally with the addition of the words "for sale" relative to conveying and furnishing of electric current for light, heat and power and the extension of petitioner's corporate life to another twenty (20) years and the increase in the rate of franchise tax from 2½% to 5%.

Respondent alleges that the income derived by petitioner from rentals of its electrical property, interest and miscellaneous electrical revenue is not covered by its franchise because these activities have no connection whatsoever with its business of "conveying and furnishing for sale of electric current for light, heat, and power" and, therefore, the said extraneous income is subject to income tax.

Petitioner is a holder of two (2) kinds of franchises, namely: (a) legislative franchise, and (b) municipal franchise. However, under Paragraph 3 of the partial stipulation of facts submitted by the parties, only the extraneous income of petitioner under the legislative franchise is contested in this case.

At the outset we hold that petitioner's exemption from all taxes and assessments under its legislative franchise is limited only to those income derived from its business covered by the franchise, i.e., furnishing and conveying for sale of electric current for light, heat, and power. All other income derived from any activity or business not specified by the franchise is subject to income tax because the consideration for the unqualified tax exemption is predicated on the payment of the franchise tax on petitioner's "gross earnings received from its business under this franchise." Consequently, any extraneous income derived from business not specified by the franchise is subject to the income tax. To hold otherwise would mean an exemption of the extraneous income from any kind of tax or assessment whatsoever which undoubtedly could not have been the intention of our legislature. Moreover, the protective mantle of income tax exemption or benefit granted by a legislative body to a franchise grantee can not be extended to the same party which chooses to descend from its high pedestal of tax preference or immunity to the level of an ordinary private corporation engaged in profitable business or undertaking. This is particularly applicable to the case at bar where the franchise grantee deviates from its contractual obligation specified under the terms of the franchise.

The legislative franchise granted to petitioner did not contemplate the acquisition or holding by petitioner of properties to be leased or rented to others for a consideration. It follows, therefore, that the franchise tax paid by petitioner on the rentals derived therefrom does not cover the exemption of petitioner from all taxes and assessments of whatever nature, including the income tax assessment in question. This view is clear and manifest from the charter itself because the objective for which petitioner was organized is "to construct, maintain and operate an electric light, heat and power system for the purpose of generating and distributing for sale electric light, heat and power." (Sec. 1, Republic Act No. 150.) The phrase "for the purpose of generating and distributing for sale electric light, heat and power" indicates that the exemption from all taxes and assessments of petitioner of its privileges, earnings, income, franchise, poles, wires, transformers and insulators, after payment of the franchise tax specified therein, is limited only to the specified activities for the proper accomplishment and operation of its enfranchised undertaking of furnishing and conveying for sale electric current for light, heat, and power. The business of generating and distributing for sale electric light, heat and power cannot, by any stretch of the imagination, include the business of leasing or renting property for a consideration. This conclusion finds support in the provision of Paragraph 9, Part Two, of petitioner's franchise, supra, which states in part that "the grantee shall pay to the City of Manila two and one-half per centum (now five per centum) of the gross earning received from the business under this franchise in the city and its suburbs x x x." It is also in accord with the ratio dicidendi laid down by the Supreme Court in the case of Manila Railroad Company vs City of Dagupan, et al., G. R. No. L-16596, April 26, 1961, 59 Off. Gaz. 6257, that:

> "The exemption from taxation of properties of the Manila Railroad Company is limited to those held by it for the proper accomplishment of its stated purpose in the franchise, i.e., 'to locate, construct, equip, maintain and operate certain railways x x x.' (See Section 1, Act 1510.) So that, where as in the instant case, the property involved are being merely rented to private individuals, the same are not exempt from taxation." (Syllabus)

In the case at bar, the business of leasing or renting properties is not included in the authorized undertaking of petitioner of generating and distributing for sale electric light, heat and power. On the contrary, the fact that a substantial portion of petitioner's properties are being rented to private persons clearly show that petitioner deviated and violated the terms and conditions inherent in the proper accomplishment and operation of its enfranchised undertaking. We do not subscribe to petitioner's view that its tax exemption under the franchise includes the power to accumulate properties for the purpose of leasing or renting them at a profit instead of devoting them to its authorized activity or business of selling, furnishing and conveying electric current for light, heat and power. (See Manila Railroad Company vs City of Dagupan, et al., _supra_.)

It is a cardinal rule in taxation that exemptions therefrom are not favored and laws granting tax exemption are to be construed in _strictissimi juris_ against the taxpayer and liberally in favor of the taxing authority (Commissioner of Internal Revenue vs Guerrero, et al., G.R. No. L-20942, Sept. 22, 1967; Philippine Acetylene Co., Inc., vs Commissioner of Internal Revenue, G.R. No. L-19707, August 17, 1967; Abad vs Court of Tax Appeals, et al., G.R. No. L-20843 and No. L-20903, October 19, 1966; Esso Standard Eastern, Inc. vs Actg. Commissioner of Customs, G.R. No. L-21841, October 28, 1966; Commissioner of Internal Revenue vs Visayan Electric Co., et al., G. R. No. L-22611, May 27, 1968; Asturias Sugar Central, Inc., vs Commissioner of Customs, et al., G. R. No. L-19337, Sept. 30, 1969). Accordingly, we are not in accord with petitioner's stand that the franchise tax of 5% on its gross earnings from the business of leasing or renting property takes the place of all taxes and assessments, including the income tax here in question.

Consequently, the extraneous income of petitioner derived from rental of its electrical property amounting to ₱188,872.00 and ₱200,114.00, or a total of ₱388,986.00, for 1960 and 1961, respectively, is subject to income tax. In the light of our holding, we rule that petitioner's miscellaneous electrical revenues of ₱34,254.00 and ₱40,444.00 for 1960 and 1961, respectively, are likewise subject to income tax in the absence of evidence that they were earned under its authorized business activity as expressed and stipulated in petitioner's legislative franchise.

The miscellaneous electrical revenue amounting to ₱34,254.00 for 1960 under the heading "legislative franchise" was not itemized. However, the income falling under the heading "municipal franchise" was broken down into rental of transformers and income from subdivision. (See p. 49, BIR records.) The other miscellaneous electrical revenue of ₱40,444.00 (₱44,850.00) for 1961, including similar income under the heading "municipal franchise", was broken down into rentals of transformers, income from subdivision, installations and removal cost, temporary lighting service and refund (see p. 16, BIR records). Again, there is no showing that these incomes were made in the course of petitioner's regular operations or transactions as indicated and specified in its enfranchised undertaking of selling, furnishing and conveying electric current for light, heat and power. On the contrary, the items of rental of transformers and income from subdivision, which comprised the bulk of these miscellaneous electrical revenues, are clearly foreign to petitioner's authorized business of generating and distributing electricity for sale.

The records of this case are not clear with respect to the nature and extent of petitioner's miscellaneous electrical revenue. They are even more incomplete and vague with respect to the character and details of petitioner's interest incomes of ₱26,796.00 and ₱31,788.00 for 1960 and 1961, respectively. On page 49 of the Bureau of Internal Revenue records, it appears that petitioner derived income from interest recorded as follows:

"From Interest
Other Income (Net)
Acct. 524.12 Am. Sch. Debt ₱2,818.00
NCB Savings Acct. 23,980.00"

From the said accounting entry, nothing is stated, expressly or impliedly, that petitioner's interest incomes were realized in the course of its regular transaction conformably with the terms of its franchise. The supporting papers which might show the meaning, details or particulars of the said entry were not presented or shown to us during the hearing of this case; neither has the entry in question been clarified in the partial stipulation of facts submitted by the parties to this Court. Our appreciation of the aforesaid entry is further confounded by the circumstance that a portion of the said income seems to be interest of an Americal School debt. (Am. Sch. Debt). With respect, however, to the interest income of petitioner in 1961 amounting to ₱31,788.00, there is absolutely nothing in the records which might indicate, directly or indirectly, the sources or details of the said income. The suppression of the details of the aforesaid entry and other accounting entries made by petitioner is indicative that the said entries, if clarified, would be against the tax interest of petitioner.

(See 5(e), Rule 131, Rules of Court).

We are aware of the ruling that the interest income on the savings accounts of a franchise holder is subject only to franchise tax provided that the source of the money deposited came exclusively from business specified in petitioner's franchise (Philippine Long Distance Telephone Company vs Collector, 90 Phil. 674; Phil. Power Dev. Co., Inc., vs Commissioner of Internal Revenue, CTA Case No. 1152, Oct. 31, 1965). In this case, however, no evidence whatsoever was presented by petitioner, either oral or documentary, which would show that such interest income came from petitioner's deposit realized from the operation of its enfranchised business which is limited to selling, conveying and furnishing electric current for light, heat and power. Considering the fact that petitioner derived substantial rental income which is foreign to its authorized business of selling, furnishing and conveying electricity, we are constrained to hold that the interest incomes of ₱26,798.00 and ₱31,788.00 for 1960 and 1961 are subject to income tax because petitioner failed to present concrete proof that such interest income represented profit arising from the specified undertaking of generating and distributing electricity for sale.

In resolving the factual question at issue, we have adopted the well-settled rule that it is incumbent upon the taxpayer to show clearly that the tax assessment is erroneous in order to be relieved from it. (Collector of Internal Revenue vs Bohol Land Transportation Co., Bohol Land Transportation Co. vs Collector of Internal Revenue, G. R. Nos. L-13099 and L-15662, April 29, 1960.) This is based on the consistent doctrine in taxation that the assessment of respondent Commissioner of Internal Revenue is <u>prima facie</u> correct and the burden of proof is upon the taxpayer to overcome the presumption of the correctness thereof. (Manila Railroad Co. vs Collector of Customs, 52 Phil. 950; José Espino vs Commissioner of Internal Revenue, CTA Case No. 1532, Jan. 21, 1969; Congregación de la Mission de San Vicente de Paul vs Commissioner of Internal Revenue, CTA Case No. 1468, May 19, 1969.) And in appeals to the Court of Tax Appeals, the determination of the Commissioner of Internal Revenue is presumed correct and it devolves upon the taxpayer to rebut such presumption. (Tan Guan vs Court of Tax Appeals, G. R. No. L-23676, April 27, 1967.) Moreover, it is a cardinal rule in taxation that a law granting tax-exemption, which is in derogation of the sovereign power of the State to tax, is not favored and cannot be presumed. Our Supreme Court has uniformly and consistently held that laws granting tax-exemption should be construed in strictissimi juris against the taxpayer and in favor of the taxing authority. (E. Rodriguez, Inc. v. Collector and CTA, G.R. No. L-23044, July 31, 1969.)

WHEREFORE, the decision of respondent appealed from is affirmed. Petitioner is hereby ordered to pay respondent or his duly authorized collection agent the sums of ₱73,727.34 and ₱80,342.30, or a total of ₱154,069.64, as deficiency income taxes and interests for 1960 and 1961, respectively. If the said amounts are not paid within thirty (30) days from the date this decision becomes final and executory, petitioner shall pay a surcharge of 5% and 1% monthly as delinquency interest on the deficiency income taxes of ₱62,480.80 and ₱68,086.70 until fully paid provided that said delinquency interest of 1% a month shall not exceed a period of three (3) years, or 36%, in accordance with Section 51(e) of the Tax Code, as amended by Republic Act No. 2343.

SO ORDERED.

Quezon City, November 22, ~~1969~~.

Estanislao R. Alvarez
ESTANISLAO R. ALVAREZ
Associate Judge

I CONCUR: Ramon L. Avanceña

RAMON L. AVANCEÑA
Associate Judge

Presiding Judge ROMAN M. UMALI did not take part.