SMART COMMUNICATIONS, INC., PETITIONER, VS. THE CITY OF DAVAO, REPRESENTED HEREIN BY ITS MAYOR HON. RODRIGO DUTERTE, AND THE SANGGUNIANG PANLUNSOD OF DAVAO CITY, RESPONDENTS.

G.R. No. 155491. July 21, 2009

Ponente: NACHURA, J.

Read online (full-text search, related cases, audio case brief): https://batas.org/library/g-r-no-155491/

NACHURA, J.:

Before the Court is a Motion for Reconsideration[1] filed by Smart Communications, Inc. (Smart) of the Decision[2] of the Court dated September 16, 2008, denying its appeal of the Decision and Order of the Regional Trial Court (RTC) of Davao City, dated July 19, 2002 and September 26, 2002, respectively.

Briefly, the factual antecedents are as follows:

On February 18, 2002, Smart filed a special civil action for declaratory relief[3] for the ascertainment of its rights and obligations under the Tax Code of the City of Davao, which imposes a franchise tax on businesses enjoying a franchise within the territorial jurisdiction of Davao. Smart avers that its telecenter in Davao City is exempt from payment of franchise tax to the City.

On July 19, 2002, the RTC rendered a Decision denying the petition. Smart filed a motion for reconsideration, which was denied by the trial court in an Order dated September 26, 2002. Smart filed an appeal before this Court, but the same was denied in a decision dated September 16, 2008. Hence, the instant motion for reconsideration raising the following grounds: (1) the "in lieu of all taxes" clause in Smart's franchise, Republic Act No. 7294 (RA 7294), covers local taxes; the rule of strict construction against tax exemptions is not applicable; (2) the "in lieu of all taxes" clause is not rendered ineffective by the Expanded VAT Law; (3) Section 23 of Republic Act No. 7925[4] (RA 7925) includes a tax exemption; and (4) the imposition of a local franchise tax on Smart would violate the constitutional prohibition against impairment of the obligation of contracts.

Section 9 of RA 7294 and Section 23 of RA 7925 are once again put in issue. Section 9 of Smart's legislative franchise contains the contentious "in lieu of all taxes" clause. The Section reads:

> Section 9. Tax provisions. -- The grantee, its successors or assigns shall be liable to pay the same taxes on their real estate buildings and personal property, exclusive of this franchise, as other persons or corporations which are now or hereafter may be required by law to pay. In addition thereto, the grantee, its successors or assigns shall pay a franchise tax equivalent to three percent (3%) of all gross receipts of the business transacted under this franchise by the grantee, its successors or assigns and the said percentage shall be in lieu of all taxes on this franchise or earnings thereof: Provided, That the grantee, its successors or assigns shall continue to be liable for income taxes payable under Title II of the National Internal Revenue Code pursuant to Section 2 of Executive Order No. 72 unless the latter enactment is amended or repealed, in which case the amendment or repeal shall be applicable thereto.
>
> xxx[5]

Section 23 of RA 7925, otherwise known as the most favored treatment clause or equality clause, contains the word "exemption," viz.:

> 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 franchises 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 the service authorized by the franchise.[6]

A review of the recent decisions of the Court on the matter of exemptions from local franchise tax and the interpretation of the word "exemption" found in Section 23 of RA 7925 is imperative in order to resolve this issue once and for all.

In Digital Telecommunications Philippines, Inc. (Digitel) v. Province of Pangasinan,[7] Digitel used as an argument the "in lieu of all taxes" clauses/provisos found in the legislative franchises of Globe,[8] Smart and Bell,[9] vis-à-vis Section 23 of RA 7925, in order to claim exemption from the payment of local franchise tax. Digitel claimed, just like the petitioner in this case, that it was exempt from the payment of any other taxes except the national franchise and income taxes. Digitel alleged that Smart was exempted from the payment of local franchise tax.

However, it failed to substantiate its allegation, and, thus, the Court denied Digitel's claim for exemption from provincial franchise tax. Cited was the ruling of the Court in PLDT v. City of Davao,[10] wherein the Court, speaking through Mr. Justice Vicente V. Mendoza, held that in approving Section 23 of RA No. 7925, Congress did not intend it to operate as a blanket tax exemption to all telecommunications entities. Section 23 cannot be considered as having amended PLDT's franchise so as to entitle it to exemption from the imposition of local franchise taxes. The Court further held that tax exemptions are highly disfavored and that a tax exemption must be expressed in the statute in clear language that leaves no doubt of the intention of the legislature to grant such exemption. And, even in the instances when it is granted, the exemption must be interpreted in strictissimi juris against the taxpayer and liberally in favor of the taxing authority.

The Court also clarified the meaning of the word "exemption" in Section 23 of RA 7925: that the word "exemption" as used in the statute refers or pertains merely to an exemption from regulatory or reporting requirements of the Department of Transportation and Communication or the National Transmission Corporation and not to an exemption from the grantee's tax liability.

In Philippine Long Distance Telephone Company (PLDT) v. Province of Laguna,[11] PLDT was a holder of a legislative franchise under Act No. 3436, as amended. On August 24, 1991, the terms and conditions of its franchise were consolidated under Republic Act No. 7082, Section 12 of which embodies the so-called "in-lieu-of-all taxes" clause. Under the said Section, PLDT shall pay a franchise tax equivalent to three percent (3%) of all its gross receipts, which franchise tax shall be "in lieu of all taxes." The issue that the Court had to resolve was whether PLDT was liable to pay franchise tax to the Province of Laguna in view of the "in lieu of all taxes" clause in its franchise and Section 23 of RA 7925.

Applying the rule of strict construction of laws granting tax exemptions and the rule that doubts are resolved in favor of municipal corporations in interpreting statutory provisions on municipal taxing powers, the Court held that Section 23 of RA 7925 could not be considered as having amended petitioner's franchise so as to entitle it to exemption from the imposition of local franchise taxes.

In ruling against the claim of PLDT, the Court cited the previous decisions in PLDT v. City of Davao[12] and

Bar review courses, mock exams and a study planner that keeps you on pace - batas.org

PLDT v. City of Bacolod,[13] in denying the claim for exemption from the payment of local franchise tax.

In sum, the aforecited jurisprudence suggests that aside from the national franchise tax, the franchisee is still liable to pay the local franchise tax, unless it is expressly and unequivocally exempted from the payment thereof under its legislative franchise. The "in lieu of all taxes" clause in a legislative franchise should categorically state that the exemption applies to both local and national taxes; otherwise, the exemption claimed should be strictly construed against the taxpayer and liberally in favor of the taxing authority.

Republic Act No. 7716, otherwise known as the "Expanded VAT Law," did not remove or abolish the payment of local franchise tax. It merely replaced the national franchise tax that was previously paid by telecommunications franchise holders and in its stead imposed a ten percent (10%) VAT in accordance with Section 108 of the Tax Code. VAT replaced the national franchise tax, but it did not prohibit nor abolish the imposition of local franchise tax by cities or municipaties.

The power to tax by local government units emanates from Section 5, Article X of the Constitution which empowers them to create their own sources of revenues and to levy taxes, fees and charges subject to such guidelines and limitations as the Congress may provide. The imposition of local franchise tax is not inconsistent with the advent of the VAT, which renders functus officio the franchise tax paid to the national government. VAT inures to the benefit of the national government, while a local franchise tax is a revenue of the local government unit.

WHEREFORE, the motion for reconsideration is DENIED, and this denial is final.

SO ORDERED.

Ynares-Santiago, (Chairperson), Chico-Nazario, Leonardo-De Castro,[*] and Bersamin,[**] JJ., concur.

---

[*] Additional member vice Justice Ruben T. Reyes (retired) per raffle dated February 23, 2009.

[**] Additional member vice Justice Alicia Austria-Martinez (retired) per raffle dated May 13, 2009.

[1] Rollo, pp. 395-436.

[2] Id. at 374-392.

[3] Rules of Court, Rule 63.

[4] Public Telecommunications Policy Act of the Philippines.

[5] Emphasis supplied.

[6] Emphasis supplied.

[7] G. R. No. 152534, February 23, 2007, 516 SCRA 541.

[8] Republic Act No. 7229.

[9] Republic Act No. 7692

[10] 415 Phil. 764 (2001).

[11] G.R. No. 151899, August 16, 2005, 467 SCRA 93.

[12] G.R. No. 143867, 415 Phil. 769, August 22, 2001; 447 Phil. 571, March 25, 2003.

Study hands-free: podcast-style lessons with read-along highlighting - batas.org

[13] G.R. No. 149179, July 15, 2005, 463 SCRA 528.

ABOUT BATAS.ORG

Study smarter at BATAS.org

The Philippine bar review and law-school companion built around how your brain actually remembers.

The complete Philippine law library - free for everyone.

More than 100,000 Supreme Court decisions, Republic Acts, and executive issuances - full-text searchable, browsable by category and year, and always free. No paywall, no login. This PDF came from it.

Audio case-brief lectures.

Any decision becomes a podcast-style lecture - facts, issues, ruling, and doctrine - with read-along highlighting and a hands-free presentation mode. Study while commuting, working out, or resting your eyes.

Bar review built on the science of memory.

Complete, sequenced courses for all eight bar subjects, narrated like podcasts and reinforced with retrieval practice and spaced review - the study techniques with the strongest evidence behind them.

The full law-school curriculum.

One subscription unlocks the entire J.D. curriculum - every subject, every lesson, with your progress tracked down to the paragraph so you can pick up exactly where you left off, on any device.

Mock exams that tell you where you stand.

Timed multiple-choice exams graded instantly, with per-subject score breakdowns and focus suggestions that point you at your weakest topics first.

A study planner that keeps you on pace.

Set your schedule and BATAS tells you every day whether you are on track for bar day - and exactly which lesson to take next.

Start free at https://batas.org

The law library is free forever - and your first lesson is one click away.

The text of this document is an official public record and remains in the public domain. Formatting, presentation, and compilation © 2026 batas.org.

Downloaded free from the batas.org Law Library. Share it freely - the library is free for every law student, bar reviewee, and practitioner.